

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-KSB

X ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934. For the fiscal year ended April 30, 2002

   TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934

Commission file number 0-22661

VECTOR ENERGY CORPORATION

(Name of small business issuer in its charter)

Texas

(State or other jurisdiction of  
incorporation or organization)

76-0582614

(I.R.S. Employer  
Identification No.)

8303 Southwest Freeway, Suite 950, Houston, Texas

(Address of principal executive offices)

77074

(Zip Code)

Registrant's telephone number, including area code: (713) 773-3284

Securities registered pursuant to Section 12(b) of the Exchange Act:

NONE

Securities registered pursuant to Section 12(g) of the Exchange Act:

Title of Each Class

Name of Each Exchange  
On Which registered

Common Stock, no par value

None

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No   .

Check if there is no disclosure of delinquent filers in response to item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.   .

State issuer's revenues for its most recent fiscal year. \$1,422,850

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was sold, or the average bid and asked price of such common equity, as of a specified date within the past 60 days. \$1,697,087 as of July 31, 2002.

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date. 62,761,071 shares of common stock, no par value, were outstanding as of July 31, 2002.

Documents Incorporated by Reference: None

Transitional Small Business Disclosure Format (Check one). Yes    No X.

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This Form 10-KSB includes “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements other than statements of historical facts included in this Form 10-KSB, including without limitation the statements under “Business”, “Properties” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” regarding the nature of the Company’s oil and gas reserves, productive wells, acreage, and drilling activities, the adequacy of the Company’s financial resources, current and future industry conditions and the potential effects of such matters on the Company’s business strategy, results of operations and financial position, are forward-looking statements. Although the Company believes that the expectations reflected in the forward-looking statements contained herein are reasonable, no assurance can be given that such expectations will prove to have been correct. Certain important factors that could cause actual results to differ materially from expectations (“Cautionary Statements”), including without limitation fluctuations of the prices received for the Company’s oil and natural gas, uncertainty of drilling results and reserve estimate, competition from other exploration, development and production companies, operating hazards, abandonment costs, the effects of governmental regulation and the leveraged nature of the Company, are stated herein in conjunction with the forward-looking statements or are included elsewhere in this Form 10-KSB. All subsequent written and oral forward-looking statements attributable to the Company or persons acting on its behalf are expressly qualified in their entirety by the Cautionary Statements.

## **PART I**

### **Item 1. Business**

#### **General**

Vector Energy Corporation (the “Company”) was incorporated under the laws of the State of Texas on June 18, 1998 as a wholly owned subsidiary of Sunburst Acquisitions II, Inc. (“Sunburst”). The Company was formed for the purpose of completing a reverse merger with Sunburst in order to change Sunburst's name to Vector Energy Corporation and its state of incorporation from Colorado to Texas. This merger was completed on June 19, 1998

Sunburst was incorporated under the laws of the State of Colorado on March 17, 1997 as a “shell” company. Sunburst’s business plan was to seek, investigate, and if warranted, acquire one or more properties or businesses, and to pursue other related activities intended to enhance shareholder value. Sunburst elected to voluntarily file a registration statement on Form 10-SB in order to become a reporting company under the Securities Exchange Act of 1934 and continued to file periodic reports required under the Exchange Act.

On May 8, 1998, Sunburst entered into an asset acquisition transaction in which it acquired substantially all of its operating assets. The transaction consisted of an Asset Purchase Agreement executed by the Company and Old Vector Corporation (formerly Vector Energy Corporation), a Texas corporation (“Old Vector”) under which Old Vector transferred substantially all of its assets to Sunburst, including its rights to two asset purchase agreements with Lisbon Development Company, L.L.C., a Texas limited liability company (“Lisbon”), and Taurus Operating, Inc., a Texas corporation (“Taurus”) dated March 23, 1998 and March 31, 1998, respectively.

Other than the rights to the above mentioned asset purchase agreements with Lisbon and Taurus, Old Vector’s assets acquired by Sunburst consisted of non-operated working interests and royalty interests in approximately 80 producing oil and gas wells located primarily in Oklahoma and Kansas. Sunburst also acquired from Old Vector a wholly owned subsidiary of Old Vector, Vector Exploration, Inc., a Texas Corporation (“Vector Exploration”), which then became a wholly owned subsidiary of Sunburst. Old Vector assigned its rights to the asset purchase agreement with Lisbon to Vector Exploration prior to Sunburst’s acquisition of Old Vector. In exchange for these assets and the rights under the asset purchase agreements, Old Vector received 100,001 shares of Common Stock.

The Company, through its newly acquired wholly owned subsidiary Vector Exploration, exercised the rights under the asset purchase agreement with Lisbon by which Vector Exploration acquired 13 oil and gas wells located in East Texas and North Louisiana. These assets are currently held in the Company’s wholly owned subsidiary Vector Exploration. In exchange for these assets, Vector Exploration delivered to Lisbon 30,000 shares of the Company’s class AA 6% cumulative convertible preferred stock (“Class AA Preferred Stock”) and assumed \$6.1 million in secured debt and \$511,465 in accounts payable, net of accounts receivable and cash acquired. The secured debt assumed by the Company is a credit facility secured by the production on the acquired producing properties that allows the Company access to a line of credit of up to \$10 million with a national bank. These liabilities, just as the assets, are held by the Company’s wholly owned subsidiary Vector Exploration. The Class AA Preferred Stock was convertible into Common Stock and voted at a rate of 100 for each share of Class AA Preferred Stock. All Class AA Preferred Stock has been converted into common stock.

The Company also exercised its rights under the asset purchase agreement with Taurus which were assigned directly to the Company, and acquired the East Westbrook Properties located in Mitchell County, Texas. In exchange for this asset, the Company issued to Taurus 213,123 shares of Common Stock.

In connection with the above transaction, the Company additionally issued 2,480,026 shares of Common Stock, a warrant to purchase an additional 300,000 shares of Common Stock at \$.10 per share, and 500,000 shares of the Company's class B preferred stock ("Class B Preferred Stock") to subscribers in exchange for an aggregate consideration of \$773,002 in cash and services. The Class B Preferred Stock is not convertible, but has 100 votes for every share of Class B Preferred.

On November 4, 1998, the Company entered into an asset acquisition transaction by which the Company acquired the right, title, and interest in certain oil, gas, and mineral leases and working interests in approximately fifteen producing oil and gas wells located in Oklahoma, Texas and Louisiana. The transaction consisted of a purchase and sale agreement with Texas Energy and Environmental, Inc. and Cougar Oil and Gas, Inc. (collectively the "Sellers").

Pursuant to the asset acquisition transaction, the Company issued 1,226,667 of its common stock to the Sellers, issued a \$120,000 non-interest bearing note payable to the Sellers, and assumed \$690,522 of the Sellers' bank debt and \$750,000 of other liabilities of the Sellers. In addition the Sellers were entitled to receive up to 500,000 additional shares of the Company's common stock based on the value of the proved developed producing reserves attributed to the properties acquired, as determined by an independent engineering evaluation on September 30, 1999. The purchase and sale agreement also required the Company to expend a minimum of \$500,000 in capital investment on the properties acquired, within nine months. If such capital investment was not made, the Sellers were entitled to receive an additional 500,000 shares of the Company's common stock. Five hundred thousand shares of common stock were issued to the Sellers on August 23, 1999. The Company does not believe any additional shares will be issued to the Sellers under this agreement.

In conjunction with the asset acquisition transaction, the Company executed an amended and restated credit agreement with its lender whereby its borrowing base was increased by \$800,000. On November 4, 1998, the Company drew down the additional \$800,000 and used the proceeds to repay the bank debt and certain of the other liabilities assumed in the asset acquisition transaction.

In addition, the Company borrowed \$500,000 from a stockholder under a six-month promissory note. Such note bore interest at 10% per annum and was subordinate to the Company's credit agreement. The holder of the promissory note received warrants to purchase 100,000 shares of the Company's common stock at \$.10 per share. Such warrants expire ten years from the date granted. On May 17, 1999 the Company issued 100,000 shares of common stock to the holder of the promissory note in order to exercise certain provisions extending the term of the note. Under the terms of the note, the Company issued an additional 200,000 shares of common stock to the holder due to its failure to pay the balance due by the extended maturity date. In December 2000, the note balance of \$500,000 and accrued interest of \$91,850 was converted into 3,945,663 shares of the Company's common stock. In addition, the holder of the promissory note exercised the warrants to purchase 100,000 shares of the Company's common stock.

On March 7, 2000, the Company closed a purchase and sale agreement with a company, which is a debtor in possession in a Chapter 11 Bankruptcy. Under the agreement, the Company acquired all of the Bankrupt Debtor's interest in a block located in the Offshore Texas, Mustang Island Area for 550,000 shares of common stock valued at \$550,000. In accordance with the

agreement, the Company immediately repurchased 16,667 shares of common stock at \$3.00 per share, for a total of \$50,000, for payment of administrative expenses in the Bankruptcy proceeding. Under the terms of the agreement, in the event that the daily rate of production from the properties acquired averages at least 5,000 Mcf per day over a complete calendar month the seller has the right to put 150,000 shares of common stock to the Company at \$3.00 per share. If the seller fails to exercise such right, the Company has the right to call 150,000 shares of common stock at \$3.00 per share. In addition, the Company may be required to issue a maximum of 370,000 additional shares of common stock to the seller based upon the required future development costs associated with the properties acquired, as determined by an independent engineering firm. In addition, the Company purchased \$120,000 in secured debt from three of the seller's secured creditors for face value.

Vector Energy Corporation and its wholly owned subsidiary, Vector Exploration, Inc., are primarily engaged in the exploration, production, acquisition and development of oil and gas properties. These operations are conducted in the United States.

### **Competitive Conditions**

The exploration, development and production of oil and gas is subject to intense competition. The principal methods of competition in the industry for the acquisition of oil and gas leases and producing properties are the payment of cash bonus payments at the time of acquisition of leases, delay rentals, location damage supplement payments, and stipulations requiring exploration and production commitments by the lessee. Producing properties are frequently offered for sale through an open competitive bidding process. Companies with greater financial resources, existing staff and labor forces, equipment for exploration, and vast experience are in a better position than the Company to compete for such leases and producing properties. In addition, the ability of the Company to market any oil and gas which it might produce could be severely limited by its inability to compete with larger companies operating in the same area, which may be drilling or able to offer any oil and gas produced at a price lower than that of the Company.

The availability of a ready market for oil and gas depends upon numerous factors beyond the Company's control, including the extent of domestic production and imports of oil and gas, proximity and capacity of pipelines, and the effect of federal and state regulation of oil and gas sales, as well as environmental restrictions on the exploration and usage of oil and gas prospects which will become even more intense in the future. The Company has a minimal competitive position in the oil and gas industry.

Raw materials requisite to the transaction of the Company's business include such items as drilling rigs and other equipment, casing pipe, drilling mud and other supplies. Such items are commonly available from a number of sources and the Company foresees no shortage or difficulty in acquiring any raw materials relevant to the conduct of its business.

### **Dependence upon one or a few major customers**

The Company currently markets the oil and gas production from its properties to nine customers, three of which represent sales in excess of 10% of the Company's total oil and gas revenues. These three customers represent approximately 35%, 20% and 11% of the Company's total oil and gas revenues, respectively. During the year ended April 30, 2001 the Company marketed the oil and gas production from its properties to nine customers, two of which represented sales in excess of 10% of the Company's total oil and gas revenues. These two customers represented approximately 39% and 18% of the Company's total oil and gas revenues, respectively. The availability of oil and gas purchasers, with respect to onshore production, is such, however, that any customer discontinuing purchases from the Company could almost assuredly be replaced by another buyer.

Approximately \$25,000,000, or 62%, of estimated future cash flows from proved reserves is related to offshore production from the Company's Mustang Island Block. Available purchasers and transportation facilities are much more limited with respect to this production. The Company has experienced significant delays in the production of its Mustang Island Block because of refusal by a pipeline to purchase its production, or allow its transportation through their facilities. The Company has recently signed a contract with the pipeline for the purchase of its production from the Mustang Island Block and production is expected to begin once required onshore compression facilities are in place.

## **Governmental and Environmental Regulations**

### *Governmental Regulations*

Domestic development, production and sale of oil and gas are extensively regulated at both the federal and state levels. Legislation affecting the oil and gas industry is under constant review for amendment or expansion, frequently increasing the regulatory burden. Also, numerous departments and agencies, both federal and state, have issued rules and regulations binding on the oil and gas industry and its individual members, compliance with which is often difficult and costly and some of which carry substantial penalties for failure to comply. State statutes and regulations require permits for drilling operations, drilling bonds and reports concerning wells. Texas and other states in which the Company conducts operations also have statutes and regulations governing conservation matters, including the unitization or pooling of oil and gas properties and establishment of maximum rates of production from oil and gas wells.

### *Environmental Regulations*

The Company's operations are subject to extensive and developing federal, state and local laws and regulations relating to environmental, health and safety matters; petroleum; chemical products and materials; and waste management. Permits, registrations or other authorizations are required for the operation of certain of the Company's facilities and for its oil and gas exploration and production activities. These permits, registrations or authorizations are subject to revocation, modification and renewal. Governmental authorities have the power to enforce compliance with these regulatory requirements, the provisions of required permits, registrations or other authorizations, and lease conditions, and violators are subject to civil and criminal penalties, including fines, injunctions or both. Failure to obtain or maintain a required permit may also result in the imposition of civil and criminal penalties. Third parties may have the right to sue to enforce compliance.

Some risk of costs and liabilities related to environmental, health and safety matters is inherent in the Company's operations, as it is with other companies engaged in similar businesses, and there can be no assurance that material costs or liabilities will not be incurred. In addition, it is possible that future developments, such as stricter requirements of environmental or health and safety laws and regulations affecting the Company's business or more stringent interpretations of, or enforcement policies with respect to, such laws and regulations, could adversely affect the Company. To meet changing permitting and operational standards, the Company may be required, over time, to make site or operational modifications at the Company's facilities, some of which might be significant and could involve substantial expenditures. There can be no assurance that material costs or liabilities will not arise from these or additional environmental matters that may be discovered or otherwise may arise from future requirements of law.

## **Employees and Consultants**

The Company has four full time employees and two part-time employees including the officers of the Company. The Company may hire additional personnel as required by its operations and may also engage the services of geological and engineering consultants from time to time to assist in its operations. The Company has recently employed engineering consultants on a part time basis.

## **Item 2. Property**

### **Properties Acquired**

#### *Lisbon Properties*

The Company acquired the Lisbon Properties on May 8, 1998, through its wholly owned subsidiary Vector Exploration, Inc. The properties consist of oil and gas working interests, ranging from approximately 50% to 100%, in eleven wells and leases in eight fields located in Gregg and Harrison Counties, Texas and Claiborne, Lincoln, Webster and Bossier Parishes, Louisiana. The primary target zones consist of the Cotton Valley, Travis Peak, Petit, Gray Sand, Haynesville, Burgess Simmons, Vaughn and Hall formations. The Company currently operates nine of the eleven wells. Currently there are nine wells producing on the properties. The aggregate amount of daily production equals approximately 300 Mcf per day (net) of natural gas and 11 barrels per day (net) of oil and condensate. On June 6, 2002, the Company closed a sale of its interest in seven of these wells (five operated and two non-operated) for total cash consideration of \$600,100.

#### *East Westbrook Properties*

The East Westbrook Properties consist of approximately a 98% working interest in 980 acres in Mitchell County, Texas that were formerly part of the East Westbrook Unit. The East Westbrook Unit encompasses approximately 1,200 acres and is part of the Westbrook Field which encompasses over 18,000 acres and has produced in excess of 99.1 million barrels of oil since its discovery in 1920. The East Westbrook Unit is located on the northeast corner of the Midland Basin Platform and on the west flank of the Eastern Shelf. The East Westbrook Unit is bordered on the west, south, and north by waterflood projects. All of these waterfloods have been infill drilled and have produced large volumes of oil. Twenty wells have been completed on the properties, five of which have recent production. The Company operates all of the wells on this property. Historically the East Westbrook Unit has been poorly managed and was placed in the hands of a promoter who went into bankruptcy. The wells were not properly maintained, no water was injected and the facility was allowed to deteriorate. Taurus acquired the property and spent nearly \$1 million putting the wells back on line, cleaning out the wells, and replacing worn equipment. In addition, the Company performed workovers on two of the wells. In order to complete the work that needs to be done to bring the property up to full production, Vector estimates that an additional \$8.1 million needs to be spent.

#### *Old Vector Properties*

The Company acquired the Old Vector Properties on May 8, 1998. The properties consist of non-operated working and royalty interests in approximately eighty wells and units located primarily in Oklahoma and Kansas. The most significant property holdings are focused in the south central, central, and northwestern regions of Oklahoma within well established producing oil and gas fields, and in a waterflood project located in Kingman County, Kansas. Because of the Company's small interest in any particular well or unit, the Company has little or no influence over the operation of the properties or their further development.

### *Texas Energy & Environmental, Inc. Properties*

The Company acquired the Texas Energy & Environmental, Inc. properties on November 4, 1998. These properties consist of fourteen wells located in Oklahoma, Texas and Louisiana. All wells are Company operated. These wells currently produce approximately 630 Mcf per day (net) and 8 barrels of oil per day (net). The Company's working interest in these wells varies from approximately 50% to 100%. The Company currently has a sale pending on five of the wells located in Oklahoma.

### *Mustang Island Block*

On March 7, 2000, the Company closed a purchase and sale agreement with a company which is a debtor in possession in Chapter 11 Bankruptcy. Under the agreement, the Company acquired all of the Bankrupt Debtor's interest in a Block located in the Offshore Texas, Mustang Island Area. The Company currently estimates that this property contains in excess of 10 Bcf of net proved reserves.

### *New Properties*

The Company continues to pursue the evaluation of a number of oil and gas properties. During their respective careers, management has made numerous contacts in the oil and gas industry and has accumulated knowledge concerning location, current ownership, and other information with respect to properties. Based on this experience and knowledge, management believes that the Company will be able to continue to acquire properties. However, additional financing will be required to pursue particular properties.

### **Other Assets**

On November 22, 2000, the Company exchanged pipeline, meter stations, and related equipment acquired in the Mustang Island transaction for a cash payment of \$150,000 and a 20% interest in Mustang Island Gathering, LLC ("the LLC") a Texas limited liability company and pipeline operator. As part of the transaction, the Company entered into a five-year natural gas purchase agreement with the LLC. As a member of the LLC, the Company has been required to guarantee a portion of the LLC's bank debt, which is approximately \$1.1 million in the aggregate. At April 30, 2002, the Company's percentage ownership in the LLC was approximately 15%. In addition, any member of the LLC has the right, but not the obligation, to transfer all of its membership units in the LLC to the Company in exchange for shares of its common stock.



## Production Information

The table below sets forth the net quantities of oil and gas production (net of all royalties, overriding royalties, and production due to others), the average sales prices, and the average production costs attributable to the Company's properties for the years ended April 30, 2002 and 2001.

|                                    | <u>Year Ended</u><br><u>April 30, 2002</u> | <u>Year Ended</u><br><u>April 30, 2001</u> |
|------------------------------------|--|--|
| <u>Net Production</u>              |  |  |
| Oil (BBLs)                         | 7,222                                      | 10,176                                     |
| Gas (MCF)                          | 372,311                                    | 377,674                                    |
| <u>Average Sales Prices</u>        |  |  |
| Oil (per BBL)                      | \$ 20.19                                   | \$ 28.62                                   |
| Gas (per MCF)                      | \$ 3.16                                    | \$ 5.40                                    |
| <u>Average Production Cost (1)</u> |  |  |
| Per Equivalent MCF of Gas (2)      | \$ 2.31                                    | \$ 2.03                                    |

(1) Production costs include lease operating expenses, severance taxes, transportation, treatment, marketing, and other direct expenses

(2) Oil production is converted to MCF using its estimated energy equivalent of six MCF per BBL

## Reserve Information

Oil and gas reserve information for the properties owned by the Company have been prepared internally by the Company.

RESERVE CALCULATIONS BY PETROLEUM ENGINEERS INVOLVE THE ESTIMATION OF FUTURE NET RECOVERABLE RESERVES OF OIL AND GAS AND THE TIMING AND AMOUNT OF FUTURE NET REVENUES TO BE RECEIVED THEREFROM. THOSE ESTIMATES ARE BASED ON NUMEROUS FACTORS, MANY OF WHICH ARE VARIABLE AND UNCERTAIN. RESERVE ESTIMATORS ARE REQUIRED TO MAKE NUMEROUS JUDGEMENTS BASED UPON PROFESSIONAL TRAINING, EXPERIENCE, AND EDUCATIONAL BACKGROUND. THE EXTENT AND SIGNIFICANCE OF THE JUDGEMENTS IN THEMSELVES ARE SUFFICIENT TO RENDER RESERVE ESTIMATES INHERENTLY IMPRECISE. SINCE RESERVE DETERMINATIONS INVOLVE ESTIMATES OF FUTURE EVENTS, ACTUAL PRODUCTION, REVENUES AND OPERATING EXPENSES MAY NOT OCCUR AS ESTIMATED. ACCORDINGLY, IT IS COMMON FOR THE ACTUAL PRODUCTION AND REVENUES LATER RECEIVED TO VARY FROM EARLIER ESTIMATES. ESTIMATES MADE IN THE FIRST FEW YEARS OF PRODUCTION FROM A PROPERTY ARE GENERALLY NOT AS RELIABLE AS LATER ESTIMATES BASED ON LONGER PRODUCTION HISTORY. RESERVE ESTIMATES BASED UPON VOLUMETRIC ANALYSIS ARE INHERENTLY LESS RELIABLE THAN THOSE BASED ON LENGTHY PRODUCTION HISTORY. ALSO, POTENTIALLY PRODUCTIVE GAS WELLS MAY NOT GENERATE REVENUE IMMEDIATELY DUE TO LACK OF PIPELINE CONNECTIONS AND POTENTIAL DEVELOPMENT WELLS MAY HAVE TO BE ABANDONED DUE TO UNSUCCESSFUL COMPLETION TECHNIQUES. HENCE, RESERVE ESTIMATES MAY VARY FROM YEAR TO YEAR.

Proved oil and gas reserves are the estimated quantities of crude oil, condensate, natural gas, and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions.

Proved developed oil and gas reserves are those reserves expected to be recovered through existing wells with existing equipment and operating methods.

The tables below set forth the estimated proved and proved developed reserves of crude oil (including condensate) and natural gas, all of which are located within the continental United States, associated with the properties owned by the Company for the years ended April 30, 2002 and 2001.

*Proved Reserves at Year End*

|                                  | Developed | Undeveloped | Total  |
|----------------------------------|-----------|-------------|--------|
| <u>Oil (BBLs) (in thousands)</u> |           |             |        |
| April 30, 2002                   | 294       | -           | 294    |
| April 30, 2001                   | 286       | 3,310       | 3,596  |
| <u>Gas (MCF) (in thousands)</u>  |           |             |        |
| April 30, 2002                   | 17,077    | -           | 17,077 |
| April 30, 2001                   | 19,070    | 1,447       | 20,517 |

*Changes in Proved Reserves*

|                                    | MCF            | BBLs      |
|------------------------------------|----------------|-----------|
|                                    | (In Thousands) |           |
| Estimated Quantity, April 30, 2000 | 31,776         | 3,857     |
| Sales of Reserves in Place         | ( 725 )        | ( 10 )    |
| Production                         | ( 378 )        | ( 10 )    |
| Changes in Estimates               | ( 10,156 )     | ( 241 )   |
| Estimated Quantity, April 30, 2001 | 20,517         | 3,596     |
| Production                         | ( 372 )        | ( 7 )     |
| Changes in Estimates               | ( 3,068 )      | ( 3,295 ) |
| Estimated Quantity, April 30, 2002 | 17,077         | 294       |

**Oil and Gas Wells**

The Company owns interests in productive oil and gas wells (including producing wells and wells capable of production), as follows:

|           | April 30, 2002     |              | April 30, 2001     |              |
|-----------|--------------------|--------------|--------------------|--------------|
|           | Gross (1)<br>Wells | Net<br>Wells | Gross (1)<br>Wells | Net<br>Wells |
| Oil Wells | 73                 | 4.39         | 73                 | 4.60         |
| Gas Wells | 47                 | 7.32         | 47                 | 8.85         |
| Total     | 120                | 11.71        | 120                | 13.45        |

(1) One or more completions in the same well are counted as one well

## Oil and gas leaseholds

The table below sets forth the Company's ownership interest in leasehold acreage. The oil and gas leases in which the Company has an interest are generally held by production. The leases may be surrendered at any time by the cessation of production.

|           | April 30, 2002 |       |             |       | April 30, 2001 |       |             |       |
|-----------|----------------|-------|-------------|-------|----------------|-------|-------------|-------|
|           | Developed (1)  |       | Undeveloped |       | Developed(1)   |       | Undeveloped |       |
|           | Acreage        |       | Acreage     |       | Acreage        |       | Acreage     |       |
|           | Gross          | Net   | Gross       | Net   | Gross          | Net   | Gross       | Net   |
| Louisiana | 6,523          | 3,311 | 8,320       | 5,073 | 6,523          | 3,535 | 8,320       | 5,073 |
| Texas     | 6,753          | 2,663 | 2,480       | 1,551 | 6,753          | 2,663 | 2,480       | 1,551 |
| Kansas    | 4,037          | 52    | 0           | 0     | 4,037          | 52    | 0           | 0     |
| Oklahoma  | 14,468         | 800   | 200         | 100   | 14,468         | 800   | 200         | 100   |
| Total     | 31,781         | 6,826 | 11,000      | 6,724 | 31,781         | 7,050 | 11,000      | 6,724 |

(1) Acres spaced or assigned to productive wells

## Office Facilities

The Company's Houston, Texas office consists of approximately 5,025 square feet and has been leased through July of 2006 for \$5,427 per month

## Item 3. Legal Proceedings

The Company is involved from time to time in various claims, lawsuits and administrative proceedings incidental to its business. In the opinion of management, the ultimate liability thereunder, if any, will not have a materially adverse effect on the financial condition or results of operations of the Company. The Company currently has accounts payable in the amount of \$1,489,383. A significant portion of these accounts are now past due and are subject to becoming matters for litigation at any time.

## Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of security holders during the fourth quarter.

## PART II

## Item 5. Market for Common Equity and Related Stockholder Matters

On June 29, 1998, the Company began trading its common stock on the NASDAQ OTC Electronic Bulletin Board under the symbol VECT. The following table shows, for the period indicated, the high and low closing bid prices of the Company common stock as reported by NASDAQ. Any market for the common stock should be considered sporadic, illiquid and highly volatile. Prices reflect inter-dealer quotations, without adjustment for retail markup, markdowns or commissions, and may not represent actual transactions.

The stock's trading range for the last two years is as follows:

|                         | <u>High</u> | <u>Low</u> |
|-------------------------|-------------|------------|
| <u>2001 Fiscal Year</u> |             |            |
| 1 <sup>st</sup> Quarter | \$ 0.63     | \$ 0.26    |
| 2 <sup>nd</sup> Quarter | 0.35        | 0.15       |
| 3 <sup>rd</sup> Quarter | 0.25        | 0.13       |
| 4 <sup>th</sup> Quarter | 0.20        | 0.11       |
| <u>2002 Fiscal Year</u> |             |            |
| 1 <sup>st</sup> Quarter | \$ 0.28     | \$ 0.12    |
| 2 <sup>nd</sup> Quarter | 0.22        | 0.10       |
| 3 <sup>rd</sup> Quarter | 0.13        | 0.04       |
| 4 <sup>th</sup> Quarter | 0.14        | 0.04       |
| <u>2003 Fiscal Year</u> |             |            |
| 1 <sup>st</sup> Quarter | \$ 0.06     | \$ 0.02    |

As of July 31, 2002, there were approximately 243 holders of record of the Company's common stock. The Company has not paid any dividends on its common stock and no dividends are anticipated in the foreseeable future. In addition, the ability of the Company to declare or pay dividends on its common stock is currently subject to certain restrictions contained in its credit facility with a bank.

#### **Item 6. Management's Discussion and Analysis**

The following discussion should be read in conjunction with the financial statements and notes thereto included elsewhere herein.

#### **Results of Operations**

Net loss increased by \$942,517, from \$1,779,692 in fiscal 2001 to \$2,722,209 in fiscal 2002. The primary cause for this increase was a reduction in sales of oil, gas and production byproducts.

Crude oil sales decreased by \$145,526 (50%), due to a combination of decreases in crude oil prices and production declines. The average sales price per barrel decreased 29% from \$28.62 in 2001 to \$20.19 in 2002. Production decreased 29% from 10,176 barrels in 2001 to 7,222 barrels in 2002.

Natural gas sales decreased by \$864,968 (42%) due to primarily to decreases in natural gas prices. The average sales price per Mcf decreased 41% from \$5.40 in 2001 to \$3.16 in 2002. The average sales price of natural gas during fiscal 2001 was unusually high due to prices which peaked at over \$9 per Mcf during the winter energy crisis. Natural gas production remained virtually unchanged, decreasing by 5,363 Mcf (1%) from 2001.

Lease operating expense increased by \$99,022 (12%) primarily due to costs associated with two leased natural gas compressors, which were added to maintain production levels. In addition, the Company incurred costs to repair a flow line leak on one of its properties and environmental costs associated with a well located in a national park.

Depletion expense increased by \$250,901 (189%). The carrying value of the Company's proved oil and gas properties are amortized on a unit-of-production basis using estimated proved oil and gas reserve quantities. Downward revisions in the Company's estimated proved reserve quantities, which were partially offset by decreased production, caused the amortization rate to increase to 2.2% in 2002 from 0.8% in 2001.

Interest expense and amortization of loan cost decreased by \$760,312 (68%) due to a combination of lower interest rates, reduced debt balances and capitalized loan costs which were fully amortized. The average interest rate on the Company's bank debt decreased from 9.94% during 2001 to 6.35% during 2002. In addition, during December 2000, \$3,000,000 of the Company's bank debt was converted into preferred stock. Interest expense in fiscal 2002 reflects the full year's effect of this reduction. Capitalized loan costs related to the Company's bank debt and production payments were fully amortized during the first quarter of 2002.

General and administrative expenses increased by \$420,253 (21%). This increase was due to an increase of \$615,430 in common stock issued for consulting fees which was partially offset by a decrease in rent expense.

### **Liquidity and Capital Resources**

On October 19, 2000, the Company sold 543,197 shares of common stock together with a warrant to purchase 543,197 shares of common stock at \$0.50 per share and an undivided 2.2% working interest in two nonproducing oil and gas wells to a private investor for a total consideration of \$100,000.00 in cash. The investor is also entitled to recoup his investment out of future production from the wells, if any. On October 19, 2000, the closing price of the common stock was \$0.24 per share. On November 24, 2000, the Company sold an undivided 1.85% interest in a nonproducing oil and gas well to the same investor for a total cash consideration of \$25,000. The investor is entitled to recoup his investment out of 50% of the future production from the well, if any. The proceeds of these transactions were used to fund development of the Mustang Island Properties.

On October 27, 2000, the Company sold 407,398 shares of common stock together with a warrant to purchase 407,398 shares of common stock at \$0.50 per share and an undivided 2.2% working interest in two nonproducing oil and gas wells to a private investor for a total consideration of \$100,000.00 in cash. The investor is also entitled to recoup his investment out of future production from the wells, if any. On October 27, 2000, the closing price of the common stock was \$0.155 per share. On November 24, 2000, the Company sold an undivided 1.85% interest in a nonproducing oil and gas well to the same investor for a total cash consideration of \$25,000. The investor is entitled to recoup his investment out of 50% of the future production from the well, if any. The proceeds of these transactions were used to fund development of the Mustang Island Properties.

Both of the transactions in October 2000 and November 2000 were treated, by the Company, as loans repayable out of production for accounting purposes. Such production loans began accruing interest on January 1, 2001 at a variable rate equal to the rate on the Company's bank debt. At April 30, 2002 and 2001 the rate was 5.75% and 8.8675%, respectively. Accrued interest on the loans totaled \$25,069 at April 30, 2002. The stock issued was booked at its fair market value and treated as a loan cost which was amortized over six months.

On December 27, 2000, the Company sold certain interest in 5 wells located in McClain, Oklahoma and undivided 10% interest in 6 wells located on the Mustang Island Property to Old Jersey Oil Ventures, LLC. for \$1,000,000.00. The brother of the President of the Company is a principal in Old Jersey Oil Ventures, LLC. At the same time Old Jersey Oil Ventures LLC, as holder of \$591,849.41 in indebtedness owed by the Company, agreed to exchange such indebtedness for 3,945,663 shares of the Company's common stock. This represented a price of \$0.15 per share. On December 27, 2000, the closing price of the common stock was \$0.125. Old Jersey Oil Ventures, LLC also exercised warrants to purchase 400,000 shares of the Company's common stock at \$0.10 per share. All shares issued to Old Jersey Oil Ventures, LLC. were issued in a private transaction and may only be transferred in a private transaction or pursuant to an applicable exemption to the registration requirements. The Company is under no obligation to register such shares. The proceeds of this transaction were used as follows: \$250,000.00 to make payments to general creditors; \$300,000.00 to make a principal payment to the lender under the Company's secured indebtedness as a condition to the lender's agreement to enter into the fifth amendment to the credit agreement described below; \$50,000 for capital investment on properties owned by the Company in St. Mary's Parish, Louisiana; and \$400,000.00 to pay principal and interest due under the Company's credit agreement.

The transaction in December 2000 was treated, by the Company, as a loan repayable out of production for accounting purposes. Such production loan began accruing interest on January 1, 2001 at a variable rate equal to the rate on the Company's bank debt. At April 30, 2002 and 2001 the rate was 5.75% and 8.8675%, respectively. Accrued interest on the loan totaled \$95,997 at April 30, 2002.

On December 27, 2000, the company entered into the Fifth Amendment to its credit agreement. As a result of that agreement, the Company's indebtedness was reduced by \$3,000,000. This indebtedness is payable in (a) three (3) monthly installments of \$31,250.00 from January 15, 2001 through March 15, 2001; (b) seven (7) monthly installments of \$125,000.00 from April 15, 2001 through October 15, 2001 and (c) a final installment of \$2,400,845.81 due November 15, 2001. No further borrowings are available. All financial covenants have been removed. As a part of this amendment, the Company issued 3,000 shares of Class A-1 Cumulative Convertible Preferred Stock to its lender in exchange for \$3,000,000 in outstanding indebtedness and pledged its interest in the Mustang Island Properties as additional collateral to the lender. Under the terms of the preferred stock, the holder of such stock is required to convert the preferred stock into shares of common stock immediately upon the registration of the common stock. Each share of preferred stock converts into an number of Initial Shares equal to \$1,000 worth of common stock at a price equal to the lesser of (i) \$0.50 per share or (ii) ninety percent (90%) of the Average Market Price. The Average Market Price is defined as the average of the highest bid and lowest asked prices of the common stock over a period of twenty-one consecutive Trading Days ending on the Trading Day immediately prior to the date of conversion. In addition, following conversion, the holder of each preferred share prior to conversion will also be entitled to receive a number of Contingent Shares equal to one hundred ten percent (110%) of the Liquidation Value of such share divided by the Average Market Price on the first anniversary of the Conversion Date minus the number of Initial Shares. The Liquidation Value is an amount equal to all declared and unpaid dividends and distributions, in any, on the preferred stock plus \$1,000. The Company is required to register the resale of the common stock with the Securities and Exchange Commission.

On November 15, 2001, the Company amended its credit agreement to change the repayment schedule to \$125,000 due on December 15, 2001 and the balance of principal and accrued but unpaid interest due on January 15, 2002.

On January 1, 2002, the Company amended its credit agreement to change the repayment schedule to \$25,000 per month in principal and interest beginning on January 31, 2002 with the balance of principal and accrued but unpaid interest due on April 15, 2002. In addition, the Company agreed to either sell, or have entered into binding agreements to sell, certain of its oil and gas properties by February 20, 2002 or to enter into a binding agreement with a nationally recognized oil and gas auction house by March 28, 2002 for the sale of such properties. All of the proceeds from the sale of such properties would be used to reduce the Company's indebtedness.

On April 1, 2002, the Company amended its credit agreement to extend the final due date of principal and accrued but unpaid interest to June 24, 2002. In addition, the date by which the Company had to enter into a binding contract with an auction house was extended to April 30, 2002.

On June 24, 2002, the Company amended its credit agreement to extend the final due date of principal and accrued but unpaid interest to July 24, 2002.

On July 24, 2002, the Company amended its credit agreement to remove the \$25,000 per month payment and to extend the final due date of principal and accrued but unpaid interest to August 24, 2002.

In accordance with the terms of the credit agreement, as amended, the Company entered into a binding contract with an auction house on two separate occasions for the sale of certain of its producing properties. On June 6, 2002, the Company closed a sale of certain of its producing properties for total cash consideration of \$600,100. Net proceeds received from the sale, which totaled \$481,027, were used to pay down the Company's bank debt. In addition, the Company currently has a sale pending on certain of its producing properties. It is anticipated that most, if not all, of the net proceeds received from this sale will be used to pay down debt.

For the past twelve months, the Company's oil and gas revenues have been sufficient to satisfy its oil and gas operating expenses and interest payments. The Company's general and administrative expenses, development costs and debt principal payments have been funded primarily from the proceeds from the sale of stock. Additional equity funding will be required to meet the current needs of the Company. Any inability of the Company to raise additional capital under such circumstances will limit the development of most of its oil and gas properties and may prevent the Company from meeting its cash requirements. The Company is currently in negotiation with its lender for a complete restructuring of its loan, which is due on August 24, 2002. In event that such a restructuring does not occur, it will be necessary for the Company to obtain new financing. If the wells currently being brought into production perform as expected such financing should be available; however, there is no assurance that such financing will in fact be available or that the wells will, in fact, perform as expected. In the absence of such well performance or financing, the company will not be able to meet its financial obligations.

The Company is currently negotiating with many of the vendors for which accounts payable were assumed in the asset acquisition transactions, and believes that a significant portion of these payables can be satisfied through the issuance of common stock.

The Company is aggressively seeking additional property acquisitions with near term revenue generating capability and future development potential. The Company is currently evaluating several potential acquisitions, which would utilize a combination of the issuance of its equity securities and additional debt financing.

## Item 7. Financial Statements

### Annual Financial Statements

The Report of the Independent Certified Public Accountants appearing at page F-3 and the Consolidated Financial Statements and Notes to Consolidated Financial Statements appearing at pages F-4 through F-21 hereof are incorporated herein by reference.

## Item 8. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None

## PART III

## Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance With Section 16(a) of the Exchange Act

The Directors and Executive Officers of the Company are as follows:

| Name                    | Age | Position   | Tenure      |
|-------------------------|-----|--|-------------|
| Samuel M. Skipper       | 43  | Director<br>Chairman of the Board<br>Chief Executive Officer | May 8, 1998 |
| Stephen F. Noser        | 56  | Director<br>President<br>Secretary<br>Assistant Treasurer    | May 8, 1998 |
| Randal B. McDonald, Jr. | 45  | Chief Financial Officer<br>Treasurer<br>Assistant Secretary  | May 8, 1998 |

All Directors of the Company will hold office until the next annual meeting of shareholders. The Executive Officers of the Company, who are appointed by the Board of Directors, hold office until their successors are chosen and qualified, or until their death, resignation or removal. The Company presently has no audit, nominating or executive committee or committees performing substantially similar functions. There are no family relationships among the Directors and Officers of the Company. The Company currently has no employment agreement with any of the Officers or Directors.

**Sam Skipper, CEO/Chairman.** Since 1990, Mr. Skipper has assisted in the consolidation of private and public companies and the entry of such companies into the public markets. From 1996 until the present, Mr. Skipper has been Managing Director of Metropolitan Capital, a boutique investment banking firm specializing in the marketing and financing of small public companies. From 1995 to 1996, Mr. Skipper served as CEO/President of Basic Natural Resources, an oil and gas company which later merged into Synaptix. In 1992, he was the founder, CEO, President and Chairman of ImageTrust, Inc., a public company which was in the diagnostic health care business. In 1990, he served as Founder and Vice President of Corporate Development of Diagnostic Health Corporation (DHC) where he assisted the company in the identification and closing of several acquisitions until DHC's acquisition by HealthSouth Corporation in 1994.



**Stephen Noser, President.** Mr. Noser has been President or Managing Director of Vector Energy since 1991. Prior to that time, he served in various management and legal capacities within the oil and gas industry. He was Vice President and General Counsel of MCO Resources, Inc. (\$60 million in assets and listed on the American Stock Exchange) from 1987 to 1988. He was Associate General Counsel and then General Counsel of Inexco Oil Company (\$500 million in assets and listed on the New York Stock Exchange) from 1983 to 1986. He also served on Inexco's Board of Directors and as a member of the company's operating committee. Both at Inexco and MCO, Mr. Noser had primary responsibility for all SEC reporting requirements and preparation of all registration statements. From 1977 to 1983, he served in various legal capacities within the American Natural Resources System. From 1974 to 1977, he served as an attorney for Mitchell Energy & Development Corp. Mr. Noser holds a B.A. from the University of St. Thomas and a J.D. degree from the University of Houston. He is a member of the Texas and Houston Bar Associations.

**Randal McDonald, Chief Financial Officer.** Mr. McDonald has twenty-two years experience in the field of public accounting. Since 1993, he has provided general financial consulting and litigation support services to a variety of companies. Such services have included preparation and review of public and private offering documents, preparation of pro forma financial statements utilized in raising capital, and services as interim chief financial officer. From 1979 to 1985, he was with KPMG Peat Marwick's Houston office, specializing in public oil and gas companies. During 1986, he served a one year rotational assignment in KPMG Peat Marwick's world headquarters developing their audit software. During 1987, he served as Chief Financial Officer for IBS Technologies, Ltd., a publicly traded computer software company. From 1988 to 1992, he was with Arthur Andersen's Denver office, specializing in public oil and gas companies. Mr. McDonald holds a B.B.A. in accounting from the University of Texas at Austin and is a licensed CPA.

The Company's three officers and directors failed to file Form 5, "Annual Statement of Beneficial Ownership of Securities", on a timely basis with the Securities and Exchange Commission. Such forms were due on or before the 45<sup>th</sup> day after the end of the Company's fiscal year and were filed concurrently with the Company's Form 10KSB

## Item 10. Executive Compensation

### Summary Compensation Table

| Name and<br>Principal Position                     | Year<br>End | Annual Compensation (1) |           |           | Long Term Compensation Awards     |                      |                  |
|--|-------------|-------------------------|-----------|-----------|-----------------------------------|----------------------|------------------|
|  |             | Salary(\$)              | Bonus(\$) | Other(\$) | Restricted<br>Stock<br>Awards(\$) | (2)(3)<br>Options(#) | All<br>Other(\$) |
| Samuel M. Skipper<br>Chief Executive Officer       | 2002        | 95,000                  | -         | -         | -                                 | -                    | -                |
|  | 2001        | 75,833                  | -         | -         | -                                 | 500,000              | -                |
|  | 2000        | 72,000                  | -         | -         | -                                 | 500,000              | -                |
| Stephen F. Noser<br>President                      | 2002        | 95,000                  | -         | -         | -                                 | -                    | -                |
|  | 2001        | 75,833                  | -         | -         | -                                 | 750,000              | -                |
|  | 2000        | 72,000                  | -         | -         | -                                 | 500,000              | -                |
| Randal B. McDonald, Jr.<br>Chief Financial Officer | 2002        | 90,000                  | -         | -         | -                                 | -                    | -                |
|  | 2001        | 75,000                  | -         | -         | -                                 | 150,000              | -                |
|  | 2000        | 72,000                  | -         | -         | -                                 | 200,000              | -                |

(1) Includes deferred compensation of \$27,000 in 2001 and \$66,000 in 2000 payable to Mr. Skipper

(2) Includes 150,000 shares of common stock issued to Mr. McDonald in 2000

(3) The options granted in 2000 were forfeited by the officers and replaced with the options granted in 2001

### Options Granted in 2002 and 2001

During the year ended April 30, 2001, Mr. Skipper was granted options to purchase 500,000 shares of the Company's common stock. These options replaced the options granted during the year ended April 30, 2000, which were forfeited by Mr. Skipper.

During the year ended April 30, 2001, Mr. Noser was granted options to purchase 750,000 shares of the Company's common stock. These options replaced the options granted during the year ended April 30, 2000, which were forfeited by Mr. Noser.

During the year ended April 30, 2001, Mr. McDonald was granted options to purchase 150,000 shares of the Company's common stock. These options replaced the options granted during the year ended April 30, 2000, which were forfeited by Mr. McDonald

### Options Exercised During 2002 and 2001 and Year End Option Values (1)

| Name                    | Number of Securities<br>Underlying Unexercised Options<br>At Fiscal Year End (#)<br>Exercisable/<br>Unexercisable | Value of Unexercised<br>In-the-Money Options<br>At Fiscal Year End (\$)<br>Exercisable/<br>Unexercisable |
|-------------------------|---|--|
| Samuel M. Skipper       | 500,000   | -  |
|                         | -   | -  |
| Stephen F. Noser        | 750,000   | -  |
|                         | -   | -  |
| Randal B. McDonald, Jr. | 150,000   | -  |
|                         | -   | -  |

(1) Since no options were exercised, no shares were acquired or value realized upon the exercise of options

At the present time, the Company has no retirement, pension or profit sharing programs for the benefit of its Directors or employees. However, at its discretion, the Company may adopt one or more of such programs in the future.

Pursuant to its bylaws and the Texas Business Corporation Act, the Company shall indemnify each Director and Officer against expenses, judgments, fines, and amounts paid in settlement actually and reasonably incurred by him in connection with any action, suit or proceeding which he may be made a party by reason of his being or having been made a Director or Officer of the Company, unless he failed to meet certain standards of conduct.

## Item 11. Security Ownership of Certain Beneficial Owners and Management

The following table sets forth certain information regarding beneficial ownership of outstanding shares as of July 31, 2001 by each person who is known by the Company to own beneficially five percent or more of the outstanding shares, the Company's Directors and Executive Officers, and all Directors and Executive Officers as a group.

| Name and Address<br>Of Beneficial Owner   | Title of Class                           | Position or Title                | Amount and Nature<br>Of Beneficial Ownership | % of<br>Class |
|---|--|----------------------------------|--|---------------|
| Samuel M. Skipper<br>8303 Southwest Freeway, Suite 950<br>Houston, Texas 77074        | Common Stock                             | Director                         | (2) 1,018,017                                | 1.6%          |
|   | Class B Preferred Stock                  | Chairman of the Board<br>CEO     | 250,000                                      | 50.0%         |
| Stephen F. Noser<br>8303 Southwest Freeway, Suite 950<br>Houston, Texas 77074         | Common Stock                             | Director, President              | (1)(3) 1,100,003                             | 1.7%          |
|   | Class B Preferred Stock                  | Secretary<br>Assistant Treasurer | 250,000                                      | 50.0%         |
| Randal B. McDonald, Jr.<br>8303 Southwest Freeway, Suite 950<br>Houston, Texas 77074  | Common Stock                             | CFO                              | (4) 300,000                                  | 0.5%          |
|   |  | Treasurer<br>Assistant Secretary |  |               |
| Eugene A. Noser, Jr.<br>90 Broad Street<br>New York, New York 10004                   | Common Stock                             | N/A                              | (1)(5) 4,945,666                             | 7.9%          |
| Wachovia Bank National Association<br>1001 Fannin, Suite 2255<br>Houston, Texas 77002 | Common Stock                             | N/A                              | (6)(7) 100,227,807                           | 61.6%         |
|   | Class A-1 Convertible<br>Preferred Stock |                                  | 3,000  | 100.0%        |
| All Officers<br>And Directors   | Common Stock                             | N/A                              | (1)(8) 2,418,020                             | 3.8%          |
|   | Class B Preferred Stock                  |                                  | 500,000                                      | 100.0%        |

- (1) Includes 50,000 shares of common stock indirectly owned by Mr. Noser because of his 50% ownership in Old Vector Corporation, which owns 100,000 shares of common stock.
- (2) Includes 500,000 shares of common stock issuable upon the exercise of stock options.
- (3) Includes 750,000 shares of common stock issuable upon the exercise of stock options.
- (4) Includes 150,000 shares of common stock issuable upon the exercise of stock options.
- (5) Includes 4,895,666 shares of common stock indirectly owned by Mr. Noser because of his control of Old Jersey Oil Ventures, L.L.C.
- (6) Includes 227,807 shares of common stock owned by First Union Investors, Inc.
- (7) Includes 100,000,000 shares of common stock issuable upon the conversion of the Class A-1 Convertible Preferred Stock, assuming a \$0.03 conversion price. See "Description of Capital Stock"
- (8) Includes 1,400,000 shares of common stock issuable upon the exercise of stock options

## Item 12. Certain Relationships and Related Transactions

The Company was obligated under a 10% promissory note payable to the brother of the Company's president. The note matured November 4, 1999 and was unsecured, except that the holder has received up 300,000 shares of the Company's common stock due event to nonpayment. In December 2000, the note balance of \$500,000 and \$91,850 in accrued interest was converted into 3,945,663 shares of the Company's common stock.

The Company's chairman and chief executive officer has executed a limited guaranty agreement covering certain deferred interest on the Company's secured line of credit. In addition, the chairman and chief executive officer made unsecured advances to the Company totaling \$86,200 and \$7,000 during the years ended April 30, 2002 and 2001, respectively.

The Company is obligated under a production payment to an entity whose principal is the brother of the Company's president. At April 30, 2002 and 2001, the balance due under such production payment was \$934,518 and \$972,875, respectively. Such production loan began accruing interest on January 1, 2001 at a variable rate equal to the rate on the Company's bank debt. At April 30, 2002 and 2001 the rate was 5.75% and 8.8675%, respectively. Accrued interest on the loan totaled \$95,997 at April 30, 2002

### **Item 13. Exhibits and Reports on Form 8-K**

Exhibits not incorporated herein by reference to a prior filing are designated by an asterisk (\*) and are filed herewith.

Exhibit 2.01 Asset Purchase Agreement between Registrant and Vector

Exhibit 2.02 Lisbon Agreement

Exhibit 2.03 Taurus Agreement

Exhibit 2.04 Agreement and Plan of Merger Between Sunburst Acquisitions II, Inc. and Vector Energy Corporation

Exhibit 3.01 Articles of Incorporation of Vector Energy Corporation

Exhibit 3.02 By-Laws of Vector Energy Corporation

Exhibit 4.01 Certificate of Designation, Preferences, Rights and Limitations of Class AA 6% Cumulative Convertible Preferred Stock and Class B Preferred Stock of Vector Energy Corporation

Exhibit 4.02 Certificate of Designation, Preferences, Rights and Limitations of Class C 5% Cumulative Convertible Preferred Stock of Vector Energy Corporation

Exhibit 21 Subsidiaries of the Registrant

Exhibit 23 Consent of Comiskey & Company\*

No reports were filed on Form 8-K during the Company's fourth fiscal quarter ended April 30, 2002.

## SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

VECTOR ENERGY CORPORATION  
(Registrant)

By /S/ Samuel M. Skipper  
Samuel M. Skipper.  
Chairman of the Board and Chief Executive Officer

Date: August 23, 2002

Pursuant to the requirements of the Securities and Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

By /S/ Stephen F. Noser  
Stephen F. Noser.  
President and Director

Date: August 23, 2002

By /S/ Randal B. McDonald, Jr.  
Randal B. McDonald, Jr.  
Chief Financial Officer  
Principal Accounting and Financial Officer

Date: August 23, 2002

**Vector Energy Corporation**  
**FINANCIAL STATEMENTS**  
**April 30, 2002 and 2001**

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## **REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS**

The Board of Directors and Stockholders of  
Vector Energy Corporation

We have audited the accompanying consolidated balance sheets of Vector Energy Corporation as of April 30, 2002 and 2001, and the related consolidated statements of income, cash flows and changes in shareholders' equity for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Vector Energy Corporation, Inc. as of April 30, 2002 and 2001, and the consolidated results of its operations, its cash flows and changes in its shareholders' equity for the years then ended in conformity with accounting principles generally accepted in the United States.

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. As more fully described in Note 11, the Company has incurred substantial losses leading to a significant working capital deficit. These and other conditions have created substantial doubt about the Company's ability to continue as a going concern. Management's assessment of these conditions and its plans to alleviate them are also described in Note 11. The accompanying financial statements do not include any adjustments which might be necessary if the Company is unable to continue.

Denver, Colorado

August 9, 2002

/s/ Comiskey & Company  
**PROFESIONAL CORPORATION**



**Vector Energy Corporation**  
**CONSOLIDATED BALANCE SHEETS**  
**April 30, 2002 and 2001**

|   | <u>April 30, 2002</u> | <u>April 30, 2001</u> |
|---|-----------------------|-----------------------|
| <b>ASSETS</b>   |                       |                       |
| <b>CURRENT ASSETS</b>   |                       |                       |
| Cash  | \$ 101,541            | \$ 781,502            |
| Cash – restricted   | -                     | 9,536                 |
| Certificates of deposit   | 100,000               | 100,000               |
| Revenue accounts receivable   | 111,747               | 420,259               |
| JIB accounts receivable   | 44,219                | 26,666                |
|   | <hr/>                 | <hr/>                 |
| <b>Total current assets</b>   | 357,507               | 1,337,963             |
|   | <hr/>                 | <hr/>                 |
| <b>PROVED OIL AND GAS PROPERTIES, USING<br/>THE FULL COST METHOD OF ACCOUNTING</b>  | 17,394,568            | 16,959,121            |
|   | <hr/>                 | <hr/>                 |
| Less accumulated depreciation, depletion,<br>Amortization, and impairment   | 962,520               | 579,091               |
|   | <hr/>                 | <hr/>                 |
| Net oil and gas properties  | 16,432,048            | 16,380,030            |
|   | <hr/>                 | <hr/>                 |
| <b>OTHER ASSETS</b>   |                       |                       |
| Other property and equipment, less accumulated<br>Depreciation of \$62,533 and \$47,485 at April 30, 2002<br>and 2001, respectively             | 44,128                | 52,627                |
| Long term accounts receivable (net of allowance for<br>Doubtful accounts of \$109,969 and \$93,136 at<br>April 30, 2002 and 2001, respectively) | 120,000               | 136,642               |
| Deferred loan costs – net   | -                     | 23,895                |
| Other assets  | 9,353                 | 6,926                 |
|   | <hr/>                 | <hr/>                 |
| <b>Total other assets</b>   | 173,481               | 220,090               |
|   | <hr/>                 | <hr/>                 |
| <b>TOTAL ASSETS</b>   | <u>\$ 16,963,036</u>  | <u>\$ 17,938,083</u>  |

**The accompanying notes are an integral part of the financial statements**

**Vector Energy Corporation**  
**CONSOLIDATED BALANCE SHEETS**  
**April 30, 2002 and 2001**

|   | <u>April 30, 2002</u> | <u>April, 30, 2001</u> |
|---|-----------------------|------------------------|
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                       |                        |
| <b>CURRENT LIABILITIES</b>  |                       |                        |
| Line of credit  | \$ 2,776,404          | \$ 3,150,846           |
| Notes payable   | 52,676                | 141,465                |
| Production payments payable to related party  | 934,518               | 972,875                |
| Production payments payable   | 250,000               | 250,000                |
| Accounts payable – trade  | 1,489,383             | 1,252,441              |
| Royalties payable   | 426,269               | 502,366                |
| Working interest revenues payable   | 69,118                | 126,824                |
| Taxes payable   | 173,702               | 162,961                |
| Advances from related parties   | 261,098               | 152,992                |
| Accrued payroll   | 106,883               | 106,883                |
| Accrued dividends payable   | 340,000               | 100,000                |
| Accrued interest  | 135,419               | 12,172                 |
|   | <hr/>                 | <hr/>                  |
| <b>Total current liabilities</b>  | 7,015,470             | 6,931,825              |
|   | <hr/>                 | <hr/>                  |
| <b>STOCKHOLDERS' EQUITY</b>   |                       |                        |
| Preferred stock class A-1, cumulative convertible;<br>\$1,000 par value per share 3,000 shares authorized;<br>3,000 shares issued and outstanding                 | 3,000,000             | 3,000,000              |
| Preferred stock class B, noncumulative nonconvertible;<br>\$1 par value per share, 500,000 shares authorized;<br>500,000 shares issued and outstanding            | 50,000                | 50,000                 |
| Common stock, no par value; 100,000,000 shares<br>authorized; 48,701,449 and 31,014,286 shares issued and<br>outstanding at April 30, 2002 and 2001, respectively | 2,653,284             | 2,476,412              |
| Additional paid-in capital  | 20,596,052            | 18,869,407             |
| Retained earnings   | ( 16,351,770)         | ( 13,389,561)          |
|   | <hr/>                 | <hr/>                  |
| <b>Total stockholders' equity</b>   | 9,947,566             | 11,006,258             |
|   | <hr/>                 | <hr/>                  |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>   | <u>\$ 16,963,036</u>  | <u>\$ 17,938,083</u>   |

The accompanying notes are an integral part of the financial statements

**Vector Energy Corporation**  
**CONSOLIDATED STATEMENTS OF INCOME**  
**Years Ended April 30, 2002 and 2001**

|   | <u>Year Ended<br/>April 30, 2002</u> | <u>Year Ended<br/>April 30, 2001</u> |
|---|--------------------------------------|--------------------------------------|
| <b>REVENUES</b>   |                                      |                                      |
| Oil Sales   | \$ 145,774                           | \$ 291,300                           |
| Gas Sales   | 1,174,764                            | 2,039,732                            |
| Production byproducts   | 29,654                               | 50,805                               |
| Other income  | 71,345                               | -                                    |
| Interest Income   | 1,313                                | 3,337                                |
|   | <hr/>                                | <hr/>                                |
| <b>Total Revenues</b>   | 1,422,850                            | 2,385,174                            |
|   | <hr/>                                | <hr/>                                |
| <b>EXPENSES</b>   |                                      |                                      |
| Production taxes  | 56,384                               | 86,053                               |
| Lease operating expense   | 902,890                              | 803,868                              |
| Depletion of oil and gas properties   | 383,430                              | 132,529                              |
| Interest expense and amortization of loan costs   | 353,323                              | 1,113,635                            |
| General and administrative expense  | 2,449,032                            | 2,028,779                            |
|   | <hr/>                                | <hr/>                                |
| <b>Total expenses</b>   | 4,145,059                            | 4,164,864                            |
|   | <hr/>                                | <hr/>                                |
| <b>Net Loss Before Cumulative Effect of Change<br/>In Accounting Principle</b>                          | ( 2,722,209)                         | ( 1,779,692)                         |
| <b>Cumulative Effect on Prior Years (to<br/>April 30, 2000) of a Change in Accounting<br/>Principle</b> | <hr/> -                              | <hr/> ( 351,460)                     |
| <b>Net Loss Before Preferred Dividend</b>   | ( 2,722,209)                         | ( 2,131,152)                         |
| <b>Preferred Stock Dividend</b>   | <hr/> 240,000                        | <hr/> 100,000                        |
| <b>NET LOSS AVAILABLE TO COMMON<br/>SHAREHOLDERS</b>  | <hr/> \$ ( 2,962,209)                | <hr/> \$ ( 2,231,152)                |
| <b>PER SHARE AMOUNTS - BASIC</b>  |                                      |                                      |
| Net Loss Before Cumulative Effect of Change<br>In Accounting Principle                                  | <hr/> \$ ( 0.08)                     | <hr/> \$ ( 0.07)                     |
| Cumulative Effect on Prior Years (to<br>April 30, 2000) of a Change in Accounting<br>Principle          | <hr/> \$ -                           | <hr/> \$ 0.01                        |
| Net Loss Available to Common Shareholders   | <hr/> \$ ( 0.08)                     | <hr/> \$ ( 0.09)                     |
| <b>WEIGHTED AVERAGE NUMBER OF<br/>SHARES OUTSTANDING</b>  | <hr/> 36,139,838                     | <hr/> 25,299,182                     |

The accompanying notes are an integral part of the financial statements

**Vector Energy Corporation**  
**CONSOLIDATED STATEMENTS OF CASH FLOW**  
**Years Ended April 30, 2001 and 2000**

|   | <u><b>Year Ended<br/>April 30, 2002</b></u> | <u><b>Year Ended<br/>April 30, 2001</b></u> |
|---|---|---|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                     |   |   |
| Net Loss  | \$ ( 2,722,209)                             | \$ ( 2,231,152)                             |
| Adjustments to reconcile net loss to net cash                   |   |   |
| Used by operating activities                                    |   |   |
| Cumulative effect of change in accounting principle             | -   | 351,460                                     |
| Depletion of oil and gas properties                             | 383,430                                     | 132,529                                     |
| Amortization expense  | 23,895                                      | 506,596                                     |
| Depreciation expense  | 15,048                                      | 20,461                                      |
| Stock issued for consulting fees                                | 1,768,600                                   | 1,153,170                                   |
| Stock issued for employee bonus                                 | 12,700                                      | -   |
| Stock options granted   | -   | 98,660                                      |
| (Increase) decrease in restricted cash                          | 9,536                                       | ( 9,536)                                    |
| (Increase) decrease in certificates of deposit                  | -   | ( 100,000)                                  |
| (Increase) decrease in accounts receivable                      | 307,601                                     | 7,899                                       |
| (Increase) decrease in other assets                             | ( 2,427)                                    | -   |
| Increase (decrease) in accounts payable                         | 359,158                                     | 176,482                                     |
| Increase (decrease) in royalties and revenues payable           | ( 133,803)                                  | 246,227                                     |
| Increase (decrease) in other current liabilities                | 133,988                                     | 178,805                                     |
| Net cash (used by) provided from operating activities           | <u>155,517</u>                              | <u>531,601</u>                              |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                     |   |   |
| Development costs incurred                                      | ( 489,652)                                  | ( 809,434)                                  |
| Sale of oil and gas properties                                  | 54,205                                      | 180,000                                     |
| Property and equipment, other                                   | ( 6,549)                                    | ( 21,567)                                   |
| Net cash (used by) provided from investing activities           | <u>( 441,996)</u>                           | <u>( 651,001)</u>                           |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                     |   |   |
| Issuance of notes payable                                       | 60,823                                      | 173,108                                     |
| Note repayments   | ( 149,612)                                  | ( 161,456)                                  |
| Borrowings under production payments                            | -   | 1,250,000                                   |
| Repayment of production payments                                | ( 38,357)                                   | ( 27,125)                                   |
| Payment on line of credit                                       | ( 374,442)                                  | ( 578,750)                                  |
| Deferred loan costs incurred                                    | -   | ( 38,893)                                   |
| Advances from related parties                                   | 108,106                                     | 7,000                                       |
| Issuance of common stock  | -   | 171,000                                     |
| Net cash (used by) provided from financing activities           | <u>( 393,482)</u>                           | <u>794,884</u>                              |
| <b>NET INCREASE (DECREASE) IN CASH<br/>AND CASH EQUIVALENTS</b> | ( 679,961)                                  | 675,484                                     |
| <b>CASH AND CASH EQUIVALENTS,<br/>BEGINNING OF PERIOD</b>       | <u>781,502</u>                              | <u>106,018</u>                              |
| <b>CASH AND CASH EQUIVALENTS,<br/>END OF PERIOD</b>             | <u>\$ 101,541</u>                           | <u>\$ 781,502</u>                           |

The accompanying notes are an integral part of the financial statements

**Vector Energy Corporation**  
**STATEMENTS OF STOCKHOLDERS' EQUITY**  
**Years Ended April 30, 2001 and 2000**

|   | Price<br><u>Per share</u> | <u>Preferred Stock</u>      |               | <u>Common Stock</u>         |               | <u>Retained<br/>Earnings</u> | <u>Paid<br/>in capital</u> | <u>Total<br/>Stockholders'<br/>Equity</u> |
|---|---------------------------|-----------------------------|---------------|-----------------------------|---------------|------------------------------|----------------------------|---|
|   |                           | <u>Number<br/>Of shares</u> | <u>Amount</u> | <u>Number<br/>of shares</u> | <u>Amount</u> |                              |                            |   |
| Balances as of April 30, 2000                                     |                           | 500,000                     | \$ 50,000     | 19,244,757                  | \$ 2,358,716  | \$ ( 11,158,409 )            | \$ 16,041,810              | \$ 7,292,117                              |
| Issued for consulting services<br>In May, 2000                    | 0.46                      |                             |               | 600,000                     | 6,000         |                              | 268,470                    | 274,470                                   |
| Issued in settlement of<br>Accounts payable<br>In May, 2000       | 0.26                      |                             |               | 129,700                     | 1,297         |                              | 32,966                     | 34,263                                    |
| Issued in settlement of<br>Notes payable<br>In May, 2000          | 0.26                      |                             |               | 170,300                     | 1,703         |                              | 43,297                     | 45,000                                    |
| Issued for consulting services<br>In June, 2000                   | 0.38                      |                             |               | 250,000                     | 2,500         |                              | 92,750                     | 95,250                                    |
| Issued for consulting services<br>In July, 2000                   | 0.33                      |                             |               | 990,000                     | 9,900         |                              | 320,400                    | 330,300                                   |
| Issued in settlement of<br>Accounts payable<br>In July, 2000      | 0.31                      |                             |               | 24,510                      | 245           |                              | 7,255                      | 7,500                                     |
| Issued for consulting services<br>In August, 2000                 | 0.23                      |                             |               | 40,000                      | 400           |                              | 8,800                      | 9,200                                     |
| Issued in settlement of<br>Accounts payable<br>In August, 2000    | 0.31                      |                             |               | 24,085                      | 241           |                              | 7,259                      | 7,500                                     |
| Issued for consulting services<br>In September, 2000              | 0.18                      |                             |               | 1,200,000                   | 12,000        |                              | 204,000                    | 216,000                                   |
| Issued in settlement of<br>Accounts payable<br>In September, 2000 | 0.20                      |                             |               | 37,313                      | 373           |                              | 7,127                      | 7,500                                     |
| Issued for consulting services<br>In October 2000                 | 0.16                      |                             |               | 400,000                     | 4,000         |                              | 60,000                     | 64,000                                    |
| Issued in settlement of<br>Accounts payable<br>In October, 2000   | 0.18                      |                             |               | 41,667                      | 417           |                              | 7,083                      | 7,500                                     |
| Issued for deferred loan costs<br>In October, 2000                | 0.20                      |                             |               | 950,595                     | 9,506         |                              | 184,008                    | 193,514                                   |
| Issued for consulting services<br>In November, 2000               | 0.14                      |                             |               | 475,000                     | 4,750         |                              | 63,700                     | 68,450                                    |

**The accompanying notes are an integral part of the financial statements**

**Vector Energy Corporation**  
**STATEMENTS OF STOCKHOLDERS' EQUITY**  
**Years Ended April 30, 2002 and 2001**

|  | Price<br><u>Per share</u> | <u>Preferred Stock</u>            |               | <u>Common Stock</u>               |               | <u>Retained</u><br><u>Earnings</u> | <u>Paid</u><br><u>in capital</u> | <u>Total</u><br><u>Stockholders'</u><br><u>Equity</u> |
|--|---------------------------|-----------------------------------|---------------|-----------------------------------|---------------|------------------------------------|----------------------------------|---|
|  |                           | <u>Number</u><br><u>Of shares</u> | <u>Amount</u> | <u>Number</u><br><u>of shares</u> | <u>Amount</u> |                                    |                                  |   |
| Issued in settlement of<br>Accounts payable<br>In November, 2000                       | 0.15                      |                                   |               | 48,701                            | 487           |                                    | 7,013                            | 7,500   |
| Issued in settlement of<br>Notes payable<br>In December, 2000                          | 0.15                      |                                   |               | 3,945,663                         | 39,457        |                                    | 552,393                          | 591,850   |
| Conversion of line of credit<br>Into preferred class A-1<br>In December, 2000          | 1,000                     | 3,000                             | 3,000,000     |                                   |               |                                    |                                  | 3,000,000   |
| Issued in settlement of<br>Accounts payable<br>In December, 2000                       | 0.17                      |                                   |               | 43,604                            | 436           |                                    | 7,064                            | 7,500   |
| Issued in settlement of<br>Accounts payable<br>In January, 2001                        | 0.15                      |                                   |               | 50,336                            | 503           |                                    | 6,997                            | 7,500   |
| Issued in settlement of<br>Accounts payable<br>In February, 2001                       | 0.14                      |                                   |               | 53,571                            | 536           |                                    | 6,964                            | 7,500   |
| Issued for consulting services<br>In March, 2001                                       | 0.19                      |                                   |               | 400,000                           | 4,000         |                                    | 73,500                           | 77,500  |
| Issued for consulting services<br>In April, 2001                                       | 0.18                      |                                   |               | 100,000                           | 1,000         |                                    | 17,000                           | 18,000  |
| Contingent consideration for<br>Acquisition of properties<br>In May thru October, 2000 | 0.39                      |                                   |               | 97,711                            | 977           |                                    | 37,070                           | 38,047  |
| Issued for development of<br>Properties in May<br>Through October, 2000                | 0.28                      |                                   |               | 727,773                           | 7,278         |                                    | 201,051                          | 208,329   |
| Sales of Common stock<br>For Cash  | 0.18                      |                                   |               | 969,000                           | 9,690         |                                    | 161,310                          | 171,000   |
| Stock options granted  |                           |                                   |               |                                   |               |                                    | 98,660                           | 98,660  |
| Cumulative effect on prior<br>years of change in<br>Accounting principle               |                           |                                   |               |                                   |               |                                    | 351,460                          | 351,460   |
| Preferred Stock Dividend   |                           |                                   |               |                                   |               | ( 100,000 )                        |                                  | ( 100,000 )   |
| Net loss   |                           |                                   |               |                                   |               | ( 2,131,152 )                      |                                  | ( 2,131,152 )   |
| Balances as of<br>April 30, 2001   |                           | 503,000                           | \$ 3,050,000  | 31,014,286                        | \$ 2,476,412  | \$ ( 13,389,561 )                  | \$ 18,869,407                    | \$ 11,006,258   |

**The accompanying notes are an integral part of the financial statements**

**Vector Energy Corporation**  
**STATEMENTS OF STOCKHOLDERS' EQUITY**  
**Years Ended April 30, 2002 and 2001**

|   | Price            | Preferred Stock  |               | Common Stock     |               | Retained          | Paid              | Total                |
|---|------------------|------------------|---------------|------------------|---------------|-------------------|-------------------|----------------------|
|   | <u>Per share</u> | <u>Number</u>    | <u>Amount</u> | <u>Number</u>    | <u>Amount</u> | <u>Earnings</u>   | <u>in capital</u> | <u>Stockholders'</u> |
|   |                  | <u>Of shares</u> |               | <u>of shares</u> |               |                   |                   | <u>Equity</u>        |
| Issued for consulting services<br>In May, 2001                  | 0.17             |                  |               | 850,000          | 8,500         |                   | 132,000           | 140,500              |
| Issued for consulting services<br>In July, 2001                 | 0.20             |                  |               | 3,020,000        | 30,200        |                   | 573,800           | 604,000              |
| Issued for consulting services<br>In August, 2001               | 0.16             |                  |               | 300,000          | 3,000         |                   | 43,500            | 46,500               |
| Issued for employee bonus<br>In October, 2001                   | 0.13             |                  |               | 100,000          | 1,000         |                   | 11,700            | 12,700               |
| Issued in settlement of<br>Accounts payable<br>In January, 2002 | 0.10             |                  |               | 457,163          | 4,572         |                   | 41,145            | 45,717               |
| Issued for consulting services<br>In January, 2002              | 0.05             |                  |               | 1,000,000        | 10,000        |                   | 40,000            | 50,000               |
| Issued for consulting services<br>In February, 2002             | 0.04             |                  |               | 1,730,000        | 17,300        |                   | 51,900            | 69,200               |
| Issued in settlement of<br>Accounts payable<br>In March, 2002   | 0.10             |                  |               | 450,000          | 4,500         |                   | 40,000            | 44,500               |
| Issued for consulting services<br>In March, 2002                | 0.12             |                  |               | 5,280,000        | 52,800        |                   | 557,600           | 610,400              |
| Issued in settlement of<br>Accounts payable<br>In April, 2002   | 0.08             |                  |               | 400,000          | 4,000         |                   | 28,000            | 32,000               |
| Issued for consulting services<br>In April, 2002                | 0.06             |                  |               | 4,100,000        | 41,000        |                   | 207,000           | 248,000              |
| Preferred Stock Dividend  |                  |                  |               |                  |               | ( 240,000 )       |                   | ( 240,000 )          |
| Net loss  |                  |                  |               |                  |               | ( 2,722,209 )     |                   | ( 2,722,209 )        |
| Balances as of<br>April 30, 2002                                |                  | 503,000          | \$ 3,050,000  | 48,701,449       | \$ 2,653,284  | \$ ( 16,351,770 ) | \$ 20,596,052     | \$ 9,947,566         |

**The accompanying notes are an integral part of the financial statements**

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements**  
**April 30, 2002 and 2001**

**1. Business and Organization**

Vector Energy Corporation, a Texas corporation (together with its subsidiary, Vector Exploration, Inc., collectively, "the Company") was formed on June 18, 1998 as a result of an agreement and plan of reorganization more fully described in Note 3. The Company is primarily engaged in the acquisition, development, production and exploration of oil and natural gas properties in the United States.

**2. Summary of Significant Accounting Policies**

**Principles of Consolidation**

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary. All significant intercompany accounts and transactions have been eliminated in consolidation.

Certain prior year amounts have been reclassified to conform with the current year presentation.

**Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Concentrations of Credit Risk**

Although the Company's accounts receivable are exposed to credit loss, the Company does not believe such risk to be significant. Most of the Company's accounts receivable are a broad and diverse group of oil and gas companies, and accordingly, do not represent a significant credit risk. In addition, the Company has accounts receivable from parties holding working interests in the Company's properties, and as such, may be collected via offset from future obligations to the parties.

The Company periodically maintains cash balances in excess of FDIC insured limits. The amount in excess at April 30, 2001 totaled \$739,000 and there was no excess at April 30, 2002.

**Oil and Gas Properties**

The Company follows the full cost method of accounting for its oil and gas properties. All costs associated with property acquisition, exploration, and development activities are capitalized in a single, United States cost center. Internal costs directly identified with the acquisition, exploration and development activities of the Company are also capitalized. Capitalized costs are amortized on the unit-of-production basis using proved oil and gas reserves. Capitalized costs are limited to the present value of estimated future net revenues less estimated future expenditures using a discount factor of ten percent. Sales and abandonments of oil and gas properties are treated as reductions of the capitalized cost pool. At April 30, 2002 and 2001, there were no costs of unproved properties or major development projects included in the capitalized cost pool.

In accordance with Statement of Financial Accounting Standards No. 121 ("SFAS 121") - Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed Of, the Company assesses the need for an impairment of capitalized costs of oil and gas properties on a combined basis, with separate consideration given to unproved properties and major development projects, of which there were none at April 30, 2001 and 2000. If impairment is indicated based upon undiscounted future cash flows, then an impairment is recognized to the extent that net capitalized costs exceed discounted expected future cash flows. No impairment was considered necessary for the years ended April 30, 2002 and 2001.



**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

**Other Property and Equipment**

Other property and equipment of the Company consists primarily of computer equipment, vehicles and furniture and fixtures, which are depreciated over estimated useful lives, ranging from three to seven years, on a straight-line basis.

**Income Taxes**

Deferred income taxes are provided to reflect the future tax consequences of differences between the tax basis of assets and liabilities and their reported amounts in the financial statements, using enacted tax rates.

**Loss Per Share**

Loss per share has been calculated using the weighted average number of shares outstanding. Outstanding warrants and other potentially dilutive securities have been excluded from the calculation of loss per share, as their effect would be anti-dilutive.

**Transactions in the Company's Stock**

Transactions in the Company's common stock are recorded at the fair value of the stock issued in the transaction, or at the value of the goods and services received, whichever is the more readily determinable amount.

**Statement of Cash Flows**

For purposes of the statement of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

The following is a summary of all significant noncash investing and financing activities and payments made for interest and income taxes for the years ended April 30, 2002 and 2001.

|  | <b><u>Year Ended</u></b><br><b><u>April 30, 2002</u></b> | <b><u>Year Ended</u></b><br><b><u>April 30, 2001</u></b> |
|--|--|--|
| <b><u>Noncash activities:</u></b>                            |  |  |
| Common stock issued for compensation                         | \$ 12,700  | \$ -   |
| Common stock issued for consulting fees                      | \$ 1,768,600   | \$ 1,153,170   |
| Common stock issued for deferred loan cost                   | \$ -   | \$ 193,514   |
| Properties acquired for stock and assumption of liabilities  | \$ -   | \$ 38,047  |
| Stock issued in settlement of accounts payable               | \$ 122,216   | \$ 94,263  |
| Stock issued in settlement of notes payable and interest due | \$ -   | \$ 636,850   |
| Stock issued for the development of oil and gas properties   | \$ -   | \$ 208,329   |
| Preferred stock issued upon the conversion of debt           | \$ -   | \$ 3,000,000   |
| <b><u>Cash Payments:</u></b>                                 |  |  |
| Interest   | \$ 206,181   | \$ 610,337   |
| Income Taxes   | \$ 0   | \$ 0   |

**3. Acquisitions of Oil and Gas Properties**

On May 8, 1998, the Company acquired various working and royalty interests in wells located in Texas, Louisiana and Oklahoma. To effect the transaction, the Company issued 30,000 shares of class AA preferred stock, valued at \$3,000,000, and 313,124 shares of common stock, valued at \$939,372. In addition, the Company assumed \$6,100,000 in bank debt and \$511,465 in accounts payable, net of accounts receivable and cash acquired. The Company capitalized \$251,704 in expenses incurred in conjunction with this transaction. Subsequently, the Company issued 116,014 shares of common stock, valued at \$163,065, for additional working interests in certain of the properties acquired.

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

On November 4, 1998, the Company acquired various working interests in wells located in Louisiana, Texas and Oklahoma. To effect the transaction, the Company issued 1,226,667 shares of common stock, valued at \$1,840,000, and a \$120,000 non-interest bearing note payable to the sellers. In addition, the Company assumed \$690,522 in bank debt and \$600,954 in accounts payable. The Company capitalized \$15,145 in expenses incurred in conjunction with this transaction. The purchase and sale agreement also provides that the sellers may receive up to 500,000 additional shares of common stock based on the value of proved developed producing reserves attributable to the properties acquired, as determined by an independent engineering evaluation as of September 30, 1999. The Company was also required to expend a minimum of \$500,000 in capital investment on the properties acquired within nine months or the sellers would be entitled to receive an additional 500,000 shares of common stock. Subsequently, the Company exchanged the working interests acquired in certain properties in Texas and \$30,000 for additional working interests in the properties acquired in Louisiana. On August 23, 1999, the Company issued 500,000 shares of common stock valued at \$1,187,500 to the sellers under the terms of the purchase and sale agreement. The Company does not believe any additional shares will be issued to the sellers under this agreement.

On March 7, 2000, the Company closed a purchase and sale agreement with a company, which is a debtor in possession in a Chapter 11 Bankruptcy. Under the agreement, the Company acquired all of the Bankrupt Debtor's interest in a block located in the Offshore Texas, Mustang Island Area for 550,000 shares of common stock valued at \$550,000. In accordance with the agreement, the Company immediately repurchased 16,667 shares of common stock at \$3.00 per share, for a total of \$50,000, for payment of administrative expenses in the Bankruptcy proceeding. Under the terms of the agreement, in the event that the daily rate of production from the properties acquired averages at least 5,000 Mcf per day over a complete calendar month the seller has the right to put 150,000 shares of common stock to the Company at \$3.00 per share. If the seller fails to exercise such right, the Company has the right to call 150,000 shares of common stock at \$3.00 per share. In addition, the Company may be required to issue a maximum of 370,000 additional shares of common stock to the seller based upon the required future development costs associated with the properties acquired, as determined by an independent engineering firm. In addition, the Company purchased \$120,000 in secured debt from three of the seller's secured creditors for face value.

On November 22, 2000, the Company exchanged pipeline, meter stations, and related equipment acquired in the Mustang Island transaction for a cash payment of \$150,000 and a 20% interest in Mustang Island Gathering, LLC ("the LLC") a Texas limited liability company and pipeline operator. As part of the transaction, the Company entered into a five year natural gas purchase agreement with the LLC. As a member of the LLC, the Company has been required to guarantee a portion of the LLC's bank debt, which is approximately \$1.1 million in the aggregate. At April 30, 2002, the Company's percentage ownership in the LLC was approximately 15%. In addition, any member of the LLC has the right, but not the obligation, to transfer all of its membership units in the LLC to the Company in exchange for shares of its common stock.

#### **4. Oil and Gas Producing Activities**

Set forth below is certain information regarding the aggregate capitalized costs of oil and gas properties, as of April 30, 2002 and 2001, and costs incurred in oil and gas property acquisition, development and exploration activities for the years ended April 30, 2002 and 2001.

|  | <u><b>April 30, 2002</b></u> | <u><b>April 30, 2001</b></u> |
|--|------------------------------|------------------------------|
| <u><b>Capitalized Costs</b></u>                      |                              |                              |
| Proved properties                                    | \$ 17,394,568                | \$ 16,959,121                |
| Unproved properties                                  | 0                            | 0                            |
| Accumulated depreciation, depletion and amortization | ( 962,520)                   | ( 579,091)                   |
|  | <u>\$ 16,432,048</u>         | <u>\$ 16,380,030</u>         |

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

|                             | <u>Year Ended</u><br><u>April 30, 2002</u> | <u>Year Ended</u><br><u>April 30, 2001</u> |
|-----------------------------|--|--|
| <b><u>Cost Incurred</u></b> |  |  |
| Property acquisitions:      |  |  |
| Proved properties           | \$ 0                                       | \$ 38,047                                  |
| Unproved properties         | 0  | 0  |
| Development costs           | 489,652                                    | 1,017,766                                  |
| Exploration costs           | 0  | 0  |
|                             | <u>\$ 489,652</u>                          | <u>\$ 1,055,813</u>                        |

The following presents the results of operations of oil and gas producing activities for the years ended April 30, 2002 and 2001:

|  | <u>Year Ended</u><br><u>April 30, 2002</u> | <u>Year Ended</u><br><u>April 30, 2001</u> |
|--|--|--|
| Oil and gas sales                        | \$ 1,350,192                               | \$ 2,381,837                               |
| Production costs                         | ( 902,890)                                 | ( 889,921)                                 |
| Exploration                              | 0  | 0  |
| Depreciation, depletion and amortization | ( 383,430)                                 | ( 132,529)                                 |
| Impairment of oil and gas properties     | 0  | 0  |
| Operating Income                         | <u>63,862</u>                              | <u>1,359,387</u>                           |
| Income tax                               | 0  | 0  |
| Net Income                               | <u>\$ 63,862</u>                           | <u>\$ 1,359,387</u>                        |

## 5. Notes Payable

Total debt at April 30, 2002 and 2001 consists of the following:

|                             | <u>April 30, 2002</u> | <u>April 30, 2001</u> |
|-----------------------------|-----------------------|-----------------------|
| Line-of-credit              | \$ 2,776,404          | \$ 3,150,846          |
| Production payments payable | 1,184,518             | 1,222,875             |
| Other                       | 52,676                | 141,465               |
|                             | <u>4,013,598</u>      | <u>4,515,186</u>      |
| Less current portion        | <u>\$ 0</u>           | <u>\$ 0</u>           |

## Line of Credit

The Company has a \$10 million revolving credit note with a national bank, which terminated on November 15, 2001. Interest on the note is payable monthly at a floating rate, which was 5.75% and 8.8675% at April 30, 2002 and 2001, respectively. The borrowing base under the note is determined periodically based upon the collateral value assigned to the mortgaged properties, and was \$2,776,404 and \$3,150,846 at April 30, 2002 and 2001, respectively. The borrowing base may be redetermined at the Bank's sole discretion. The Company does not anticipate that the borrowing base under the note can be increased without incurring significant development costs.

On December 27, 2000, the Company amended its credit agreement to reduce its indebtedness by \$3,000,000, reschedule principle payments, and remove all financial covenants. Under the terms of the amended credit agreement, the indebtedness was payable in three monthly installments of \$31,250 beginning on January 15, 2001, seven monthly installments of \$125,000 beginning on April 15, 2001, and a final installment of \$2,400,846 due on November 14, 2001. No further borrowings are available. As part of the amended credit agreement, the Company issued 3,000 shares of Class A-1 Cumulative Convertible Preferred Stock to the bank in exchange for \$3,000,000 in outstanding indebtedness and pledged its interest in the Mustang Island properties as additional collateral under the loan.

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

On November 15, 2001, the Company amended its credit agreement to change the repayment schedule to \$125,000 due on December 15, 2001 and the balance of principal and accrued but unpaid interest due on January 15, 2002.

On January 1, 2002, the Company amended its credit agreement to change the repayment schedule to \$25,000 per month in principal and interest beginning on January 31, 2002 with the balance of principal and accrued but unpaid interest due on April 15, 2002. In addition, the Company agreed to either sell, or have entered into binding agreements to sell, certain of its oil and gas properties by February 20, 2002 or to enter into a binding agreement with a nationally recognized oil and gas auction house by March 28, 2002 for the sale of such properties. All of the proceeds from the sale of such properties would be used to reduce the Company's indebtedness.

On April 1, 2002, the Company amended its credit agreement to extend the final due date of principal and accrued but unpaid interest to June 24, 2002. In addition, the date by which the Company had to enter into a binding contract with an auction house was extended to April 30, 2002.

On June 24, 2002, the Company amended its credit agreement to extend the final due date of principal and accrued but unpaid interest to July 24, 2002.

On July 24, 2002, the Company amended its credit agreement to remove the \$25,000 per month payment and to extend the final due date of principal and accrued but unpaid interest to August 24, 2002.

The Company is currently in negotiation with its lender for a complete restructuring of its loan. In the event that such a restructuring does not occur, it will be necessary for the Company to obtain new financing.

In accordance with the terms of the credit agreement, as amended, the Company entered into a binding contract with an auction house on two separate occasions for the sale of certain of its producing properties. On June 6, 2002, the Company closed a sale of certain of its producing properties for total cash consideration of \$600,100. Net proceeds received from the sale, which totaled \$481,027, were used to pay down the Company's bank debt. In addition, the Company currently has a sale pending on certain of its producing properties. It is anticipated that most, if not all, of the net proceeds received from this sale will be used to pay down debt.

#### **Certificates of Deposit**

At April 30, 2002 and 2001, the Company had three certificates of deposit totaling \$100,000. Such certificates bore interest at rates ranging from 1.883% to 1.982% at April 30, 2002 and 4.554% to 4.746 % at April 30, 2001. The maturity dates of the certificates ranged from February 19, 2003 to March 20, 2003 at April 30, 2002 and from October 27, 2001 to April 3, 2002 at April 30, 2001. The certificates of deposit are collateral for three letters of credit, with expiration dates corresponding to the maturity dates of the certificates, issued in favor of governmental agencies in states in which the Company operates wells. It is anticipated that such certificates of deposit and the corresponding letters of credit will be renewed at maturity.

#### **Production Payments Payable**

On October 19, 2000, the Company sold 543,197 shares of common stock together with a warrant to purchase 543,197 shares of common stock at \$0.50 per share and an undivided 2.2% working interest in two nonproducing oil and gas wells to a private investor for a total consideration of \$100,000.00 in cash. The investor is also entitled to recoup his investment out of future production from the wells, if any. On October 19, 2000, the closing price of the common stock was \$0.24 per share. On November 24, 2000, the Company sold an undivided 1.85% interest in a nonproducing oil and gas well to the same investor for a total cash consideration of \$25,000. The investor is entitled to recoup his investment out of 50% of the future production from the well, if any. The proceeds of these transactions were used to fund development of the Mustang Island Properties.

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

On October 27, 2000, the Company sold 407,398 shares of common stock together with a warrant to purchase 407,398 shares of common stock at \$0.50 per share and an undivided 2.2% working interest in two nonproducing oil and gas wells to a private investor for a total consideration of \$100,000.00 in cash. The investor is also entitled to recoup his investment out of future production from the wells, if any. On October 27, closing price of the common stock was \$0.155 per share. On November 24, 2000, the Company sold an undivided 1.85% interest in a nonproducing oil and gas well to the same investor for a total cash consideration of \$25,000. The investor is entitled to recoup his investment out of 50% of the future production from the well, if any. The proceeds of these transactions were used to fund development of the Mustang Island Properties.

Both of the transactions in October 2000 and November of 2000 were treated, by the Company, as loans repayable out of production for accounting purposes. Such production loans began accruing interest on January 1, 2001 at a variable rate equal to the rate on the Company's bank debt. At April 30, 2002 and 2001 the rate was 5.75% and 8.8675%, respectively. Accrued interest on the loans totaled \$25,094 at April 30, 2002. The stock issued was booked at its fair market value and treated as a loan cost which was amortized over six months.

On December 27, 2000, the Company sold certain interest in 5 wells located in McClain County, Oklahoma and undivided 10% interest in 6 wells located on the Mustang Island Property to Old Jersey Oil Ventures, LLC. for \$1,000,000.00. The brother of the President of the Company is a principal in Old Jersey Oil Ventures, LLC. At the same time Old Jersey Oil Ventures LLC, as holder of \$591,849.41 in indebtedness owed by the Company, agreed to exchange such indebtedness for 3,945,663 shares of the Company's common stock. This represented a price of \$0.15 per share. On December 27, 2000, the closing price of the common stock was \$0.125. Old Jersey Oil Ventures, LLC also exercised warrants to purchase 400,000 shares of the Company's common stock at \$0.10 per share. All shares issued to Old Jersey Oil Ventures, LLC. were issued in a private transaction and may only be transferred in a private transaction or pursuant to an applicable exemption to the registration requirements. The Company is under no obligation to register such shares. The proceeds of this transaction were used as follows: \$250,000.00 to make payments to general creditors; \$300,000.00 to make a principal payment to the lender under the Company's secured indebtedness as a condition to the lender's agreement to enter into the fifth amendment to the credit agreement described above; \$50,000 for capital investment on properties owned by the Company in St. Mary's Parish, Louisiana; and \$400,000.00 to pay principal and interest due under the Company's credit agreement. Old Jersey Oil Ventures, LLC is entitled to recoup its investment out of future production from the wells in McClain County, Oklahoma and on the Mustang Island Property.

The transaction in December 2000 was treated, by the Company, as a loan repayable out of production for accounting purposes. Such production loan began accruing interest on January 1, 2001 at a variable rate equal to the rate on the Company's bank debt. At April 30, 2002 and 2001 the rate was 5.75% and 8.8675%, respectively. Accrued interest on the loan totaled \$95,997 at April 30, 2002.

**Other notes payable**

The Company was obligated under an unsecured non-interest bearing promissory note, payable in equal monthly installments of \$10,000 per month. The outstanding balance on this note was \$45,000. In May 2000, the balance of the note was converted into 170,300 shares of the Company's common stock

Other notes payable at April 30, 2002 consisted of \$18,506 in unsecured 9% to 10.5% notes issued to vendors in settlement of accounts payable. The notes are past their due dates and are due on demand. Also included is a \$34,170 financing obligation for insurance premiums, payable in monthly installments, with interest at 6.76%, through March 2003.

**6. Income Taxes**

The Company has available at April 30, 2002 an approximate \$12,000,000 unused operating loss carryforward that may be applied against future taxable income, and that expires in the years 2013 and 2019 through 2022.. Temporary deductible tax differences exist between depletion for financial statement purposes and depletion for tax purposes. The tax benefit of unused operating loss carryforwards and deductible temporary differences of approximately \$4,000,000 has been offset by a full valuation allowance. The valuation allowance increased by approximately \$300,000 for the year ended April 30, 2002.

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

## **7. Stockholder's Equity**

### **Preferred Stock**

The Company is authorized to issue 3,000 shares of Class A-1 Cumulative Convertible Preferred Stock (Class A-1 Preferred Stock). Class A-1 Preferred Stock was issued for \$1,000 per share and is entitled to receive cumulative cash dividends at the annual rate of 8% payable annually in arrears commencing December 1, 2001 when and as declared by the Board of Directors. All shares of Class A-1 Preferred Stock were issued to the Company's secured lender on December 27, 2000 as consideration for the reduction in the Company's secured indebtedness by \$3,000,000.00 and remain outstanding. The Class A-1 Preferred Stock will convert to common stock upon the effective date of its registration. Each share of Class A-1 Preferred Stock will convert into shares of the Company's common stock equal to \$1,000.00 per share plus all accumulated and unpaid dividends (the "Liquidation Value") divided by the lesser of \$0.50 or 90% of the average of the highest bid and lowest asked prices of the common stock over a period of twenty-one consecutive trading days ending on the trading day immediately prior to the date of conversion. In addition, on the first anniversary of the conversion, each holder may be entitled to receive additional shares ("Contingent Shares") equal to 110% of the Liquidation Value divided by the average of the highest bid and lowest asked prices of the common stock over a period of twenty-one consecutive trading days ending on the trading day immediately prior to the first anniversary date of such conversion minus the shares received by such holder upon the conversion. If the computation of Contingent Shares results in a negative number then no Contingent Shares shall be issued. Each share of Class A-1 Preferred Stock is entitled to cast a number of votes equal to the number of shares of common stock into which the Class A-1 Preferred Stock is convertible. The Class A-1 Preferred Stock is senior to all other series of preferred stock and all of the Company's common stock. At April 30, 2002 and 2001, cumulative preferred dividends in arrears totaled \$340,000 and \$100,000, or \$0.11 and \$0.03 per share, respectively.

The Company is authorized to issue 500,000 shares of Class B Preferred Stock, par value \$1.00 per share. The holders of Class B Preferred Stock are not entitled to receive any dividends. As of April 30, 2002 and 2001, 500,000 shares of the Class B Preferred Stock were issued and outstanding. The Class B Preferred Stock is redeemable in whole, but not in part, at the option of the Corporation by resolution of the Corporation's Board of Directors at anytime at \$1.00 per share. Each share of Class B Preferred Stock has the voting rights equal to 100 shares of the Company's common stock. The holders of Class B shares are entitled to elect at least two directors to the Board of Directors of the Corporation. The holders of Class B Preferred Stock voting as a class will have the right to remove without cause at any time and replace any director such holders have elected.

### **Common Stock**

The Company has 100,000,000 shares of authorized common stock, of which 48,701,449 and 31,014,286 shares were issued and outstanding at April 30, 2002 and 2001, respectively.

### **Stock Options and Warrants**

The Company applied Accounting Principles Board No. 25, Accounting for Stock Issued to Employees, and related interpretations in accounting for options granted prior to August 2000. In August 2000, the Company implemented the provisions of Statement of Financial Accounting Standards No. 123, Accounting for Stock Based Compensation (SFAS No. 123) using a Black Scholes option pricing model. Accordingly, the Company recognized \$98,660 in compensation cost during the year ended April 30, 2001 for options granted.

The table following presents the assumptions used in calculating the fair value of the options granted.

|                          | <u><b>2001</b></u> |
|--------------------------|--------------------|
| <b>Assumptions Used:</b> |                    |
| Expected Life (Years)    | 3                  |
| Stock Volatility         | 275% to 285%       |
| Dividends                | None               |
| Risk Free Interest Rate  | 5.00% to 6.37%     |

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

The following is a summary of option activity for the years ended April 30, 2002 and 2001.

|                                       | Weighted<br>Shares<br>Under<br>Option | Average<br>Exercise<br>Price | Options<br>Exercisable | Weighted<br>Average<br>Exercise<br>Price |
|---------------------------------------|---------------------------------------|------------------------------|------------------------|--|
| Options outstanding at April 30, 2000 | 1,742,000                             | \$ 0.64                      | 1,742,000              | \$ 0.64                                  |
| Options cancelled                     | ( 1,742,000)                          | 0.64                         | ( 1,742,000)           | 0.64                                     |
| Options granted                       | 2,080,000                             | 0.22                         | 2,080,000              | 0.22                                     |
| Options outstanding at April 30, 2001 | 2,080,000                             | 0.22                         | 2,080,000              | 0.22                                     |
| Options granted                       | -                                     | -                            | -                      | -  |
| Options outstanding at April 30, 2002 | <u>2,080,000</u>                      | \$ 0.22                      | <u>2,080,000</u>       | \$ 0.22                                  |

All of the above options are fully vested, and expire during the year ended April 30, 2006.. The options, which were issued at a price equal to or exceeding the market value of the underlying stock on the date of the grant, are not intended to qualify as incentive stock options under Internal Revenue Code Section 422.

In December 2000, warrants for the purchase of 400,000 shares of the Company's common stock were exercised at a purchase price of \$0.10 per share. In October 2000, the Company sold warrants to two investors to purchase 950,595 shares of the Company's common stock at the purchase price of \$0.50 per share. These warrants may be exercised at any time until their expiration on October 19, 2003 and are transferable and are the only warrants outstanding at April 30, 2002 and 2001

## **8. Significant Customers**

The Company currently markets the oil and gas production from its properties to nine customers, three of which represent sales in excess of 10% of the Company's total oil and gas revenues. These three customers represent approximately 35%, 20% and 11% of the Company's total oil and gas revenues, respectively. During the year ended April 30, 2001 the Company marketed the oil and gas production from its properties to nine customers, two of which represented sales in excess of 10% of the Company's total oil and gas revenues. These two customers represented approximately 39% and 18% of the Company's total oil and gas revenues, respectively. The availability of oil and gas purchasers, with respect to onshore production, is such, however, that any customer discontinuing purchases from the Company could almost assuredly be replaced by another buyer.

Approximately \$25,000,000, or 62%, of estimated future cash flows from proved reserves is related to offshore production from the Company's Mustang Island Block. Available purchasers and transportation facilities are much more limited with respect to this production. The Company has experienced significant delays in the production of its Mustang Island Block because of refusal by a pipeline to purchase its production, or allow its transportation through their facilities. The Company has recently signed a contract with the pipeline for the purchase of its production from the Mustang Island Block and production is expected to begin once required onshore compression facilities are in place.

## **9. Related Party Transactions**

During the years ended April 30, 2002 and 2001, an officer, director and shareholder of the Company made unsecured advances totaling \$108,106 and \$7,000, respectively, to the Company.

The Company is obligated under a production payment to an entity whose principal is the brother of the Company's president. At April 30, 2002 and 2001 the balance due under such production payment was \$934,518 and \$972,875, respectively. Such production loan began accruing interest on January 1, 2001 at a variable rate equal to the rate on the Company's bank debt. At April 30, 2002 and 2001 the rate was 5.75% and 8.8675%, respectively. Accrued interest on the loan totaled \$95,997 at April 30, 2002.

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

**10. Commitments and Contingencies**

Rent expense for the years ended April 30, 2002 and 2001 was \$63,896 and \$101,911, respectively. In June 2001, the Company entered into a long-term lease for office space at an annual rent of \$65,124. As of April 30, 2002, future minimum lease payments under this lease were as follows:

|       |    |                |
|-------|----|----------------|
| 2003  | \$ | 65,124         |
| 2004  |    | 65,124         |
| 2005  |    | 65,124         |
| 2006  |    | 65,124         |
| 2007  |    | 21,708         |
| Total | \$ | <u>282,204</u> |

**11. Going Concern**

As shown in the financial statements, the Company incurred net losses of approximately \$2,700,000 and \$2,100,000 for the years ended April 30, 2002 and 2001, respectively. Current liabilities exceeded current assets by approximately \$6,658,000 and \$5,594,000 at April 30, 2002 and 2001, respectively. Amounts outstanding and payable to creditors are in arrears and the Company is in negotiations with creditors to obtain extensions and settlements of outstanding amounts. Of the \$9,947,566 and \$11,006,258 in shareholders' equity at April 30, 2002 and 2001, respectively, \$16,432,048 and \$16,380,030, respectively, is attributable to the Company's investment in oil and gas properties. Management anticipates that significant additional expenditures will be necessary to develop the properties, which consist of only proved reserves, before significant positive operating cash flows will be achieved. These factors are an indication that the Company may be unable to continue in existence.

Management's plans to alleviate these conditions include the renegotiation of certain trade payables, settlements of debt amounts with stock, deferral of certain time payments, and sales of properties, as considered necessary by management. In addition, management is pursuing business partnering arrangements for the acquisition and development of additional properties as well as debt and equity funding through private placements.

The accompanying financial statements are prepared as if the Company will continue as a going concern. They contain none of the adjustments, including adjustments to recorded assets and liabilities, which might be necessary if the Company were unable to continue.

**12. Change in Accounting Principle**

In the third quarter of fiscal 2001, the Company elected to adopt effective for all of fiscal 2001 and future years the accounting provisions of SFAS No. 123 (Accounting for Stock Based Compensation) as it pertains to options issued to employees. The net loss for fiscal 2001 includes the cumulative effect [(\$351,460) net of tax of \$0, or (\$0.01) per share] necessary to adjust the Company's recorded compensation for all options issued to employees prior to fiscal 2001.

**13. Subsequent Events**

On June 6, 2002, the Company closed a sale of certain of its producing properties located in Texas and Louisiana for total cash consideration of \$600,100. Expenses relating to the sale were \$42,005 and \$77,068 of the proceeds was used to pay certain outstanding liabilities related to the properties. The remaining net proceeds of \$481,027 was used to pay down the Company's bank debt.

The Company also has a sale pending on its producing properties located in Oklahoma. The Company anticipates that most, if not all, of any proceeds realized from this sale will be used to pay down debt.



**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

**14. Oil and Gas Reserve Information (Unaudited)**

The estimates of proved oil and gas reserves utilized in the preparation of the financial statements were estimated by the Company in accordance with guidelines established by the Securities and Exchange Commission and the Financial Accounting Standards Board, which require that reserve reports be prepared under existing economic and operating conditions with no provision for price and cost escalation except by contractual agreement. All of the Company's reserves are located in the continental United States.

Future prices received for production and future production costs may vary, perhaps significantly, from the prices and costs assumed for purposes of these estimates. There can be no assurance that the proved reserves will be developed within the periods indicated or that prices and costs will remain constant. There can be no assurance that actual production will equal the estimated amounts used in the preparation of reserve projections. In accordance with the Securities and Exchange Commission's guidelines, the Company's internal petroleum engineers' estimates of future net cash flows from the Company's proved properties and the present value thereof are made using oil and natural gas sales prices in effect as of the dates of such estimates and are held constant throughout the life of the properties. Average prices used in estimating the future net cash flows were \$21.55 per barrel of oil and \$3.17 per Mcf of gas and \$23.17 per barrel of oil and \$5.59 per Mcf of natural gas at April 30, 2002 and 2001, respectively.

There are numerous uncertainties inherent in estimating quantities of proved reserves and in projecting future rates of production and timing of development expenditures. Oil and gas reserve engineering must be recognized as a subjective process of estimating underground accumulations of oil and gas that cannot be measured in an exact way, and estimates of other engineers might differ materially from those shown below. The accuracy of any reserve estimate is a function of the quality of available data and engineering and geological interpretation and judgment. Results of drilling, testing and production after the date of the estimate may justify revisions. Accordingly, reserve estimates are often materially different from the quantities of oil and gas that are ultimately recovered. Reserve estimates are integral in management's analysis of impairments of oil and gas properties and the calculation of depreciation, depletion and amortization on those properties.

|                                       | Oil<br>(Bbls)  | Gas<br>(Mcf) |
|---------------------------------------|----------------|--------------|
|                                       | (in thousands) |              |
| <u>Proved Reserves</u>                |                |              |
| Estimated Quantities – April 30, 2000 | 3,857          | 31,776       |
| Sales of Reserves in Place            | ( 10)          | ( 725)       |
| Production                            | ( 10)          | ( 378)       |
| Revisions                             | ( 241)         | ( 10,156)    |
| Estimated Quantities – April 30, 2001 | 3,596          | 20,517       |
| Production                            | ( 7)           | ( 372)       |
| Revisions                             | ( 3,295)       | ( 3,068)     |
| Estimated Quantities – April 30, 2002 | 294            | 17,077       |
| <u>Proved Developed Reserves</u>      |                |              |
| April 30, 2002                        | 294            | 17,077       |
| April 30, 2001                        | 286            | 19,070       |

**Vector Energy Corporation**  
**Notes to Consolidated Financial Statements (Continued)**  
**April 30, 2002 and 2001**

Standardized Measure of Discounted Future Net Cash Flows Relating to Proved Oil and Gas Reserves:

|   | As of April 30, |            |
|---|-----------------|------------|
|   | 2002            | 2001       |
|   | (in thousands)  |            |
| Future cash inflows   | \$ 60,378       | \$ 190,982 |
| Future production costs                                     | ( 16,754)       | ( 31,740)  |
| Future development costs                                    | ( 2,897)        | ( 15,212)  |
| Future net cash flows                                       | 40,727          | 144,030    |
| 10% annual discount for estimating<br>Timing of cash flows  | ( 11,328)       | ( 74,433)  |
| Standardized measure of discounted<br>Future net cash flows | \$ 29,399       | \$ 69,597  |

Changes in Standardized Measure of Discounted Future Net Cash Flows Relating to Proved Oil and Gas Reserves:

|  | Year Ended of April 30, |           |
|--|-------------------------|-----------|
|  | 2002                    | 2001      |
|  | (in thousands)          |           |
| Standardized measure of discounted<br>Future net cash flows, beginning of year | \$ 69,597               | \$ 74,513 |
| Changes due to operations:   |                         |           |
| Sales, net of production costs   | ( 391)                  | ( 1,492)  |
| Net change in prices, net of production costs                                  | ( 24,228)               | 47,353    |
| Development costs incurred   | 490                     | 1,018     |
| Change in future development costs   | 2,034                   | ( 1,675)  |
| Revisions of quantity estimates  | ( 28,580)               | ( 36,624) |
| Sales of Reserves  | -                       | ( 2,608)  |
| Changes in production rates, timing and other                                  | 3,517                   | ( 18,339) |
| Accretion of discount  | 6,960                   | 7,451     |
| Standardized measure of discounted<br>Future net cash flows, end of year       | \$ 29,399               | \$ 69,597 |

In August, 2002, the Company closed a sale of certain of its producing wells located in Texas and Louisiana, effective as of July 1, 2002. In addition, the Company has a sale pending on its producing wells located in Oklahoma, to be effective as of July 1, 2002. Reserve information related to wells which have been sold, or have sales pending, which has been included in the disclosures above is as follows as of April 30, 2002:

|                        | Oil<br>(Bbls)  | Gas<br>(Mcf) |
|------------------------|----------------|--------------|
|                        | (in thousands) |              |
| <u>Proved Reserves</u> |                |              |
| Proved Developed       | 65             | 863          |
| Proved Undeveloped     | -              | -            |
| Total Proved Reserves  | 65             | 863          |

|                                      | In Thousands |
|--------------------------------------|--------------|
| Future Net Cash Flows - Undiscounted | \$ 2,368     |
| Future Net Cash Flows - Discounted   | \$ 1,363     |